Fitch Ratings

Global Economic Outlook – June 2023

Central Bank Inflation Fight Continues

Global Economic Outlook – June 2023

Central Bank Inflation Fight Continues

> "Monetary policy tightening is taking a bit longer to feed through to the real economy than many expected, but there are no grounds for believing that economies have become immune to rate rises".
>
> Brian Coulton, Chief Economist, Fitch Ratings

World economic activity is holding up better than expected and Fitch Ratings has raised its forecast for global GDP growth in 2023 to 2.4%, from 2.0% in the March *Global Economic Outlook* (GEO).

The biggest upgrades have been to emerging markets (EM) where incoming data have been a lot stronger than expected. We have revised up EM ex-China growth for 2023 to 2.9% from 2.0% with Brazil, India, Mexico and Russia seeing substantive improvements. We have raised China's 2023 forecast to 5.6% from 5.2% after a swifter-than-expected reopening rebound in 1Q23. The recovery has faltered somewhat in recent months but consumption continues to normalise and macro policy is starting to be eased.

We have also raised our US growth forecast for 2023 to 1.2% from 1.0% as consumption and job growth remain robust. We still expect Fed tightening to push the economy into a mild recession, but the timing of this has been pushed out to 4Q23-1Q24. Our US growth forecast for 2024 has, accordingly, been cut to 0.5% from 0.8%. Eurozone growth forecasts for 2023 and 2024 are unchanged.

We have lowered our world GDP forecast for 2024 to 2.1% from 2.4% in March, due to longer lags in the impact of higher interest rates, along with weaker base effects for EM growth. World growth should pick up in 2025 on monetary easing in 2024.

Core Inflation Is Proving Sticky

Headline inflation has fallen but core inflation remains stubbornly high. Goods inflation has fallen but this has been offset by rising services inflation. Wage growth in the US and Europe far exceeds rates consistent with inflation targets as labour markets stay tight.

Interest Rates Higher for Longer

Advanced country central banks have become more concerned about inflation persistence and our policy rate forecasts have been revised up widely. We now expect the Fed and ECB to raise rates two more times in the coming months, to peaks of 5.75% and 4.5%, respectively. And we now anticipate three more hikes from the Bank of England (BOE), taking rates to 5.25%. No subsequent cuts are expected until 2024. In EM, by contrast, China recently cut rates and Brazil and Mexico are expected to cut later this year.

Long and Variable Lags

Low unemployment, savings buffers accumulated during the Covid-19 pandemic and easing supply shocks have contributed to recent growth resilience. But monetary tightening is gaining traction and increasingly will weigh on US and European demand over time. World trade and manufacturing are already slowing sharply.

Risks from Credit Tightening

There was no credit crunch in the aftermath of recent US banking stresses but bank funding costs are rising. And with central bank quantitative tightening (QT) policies withdrawing liquidity, there is a risk of sharper-than-expected credit tightening hitting growth.

Related Research

Global Economic Outlook (March 2023)

U.S. Consumption Boost from Pandemic Savings Will Soon Fade (June 2023)

Sticky UK Inflation Piles Pressure on BOE (May 2023)

Analysts


Brian Coulton
+44 20 3530 1140
brian.coulton@fitchratings.com

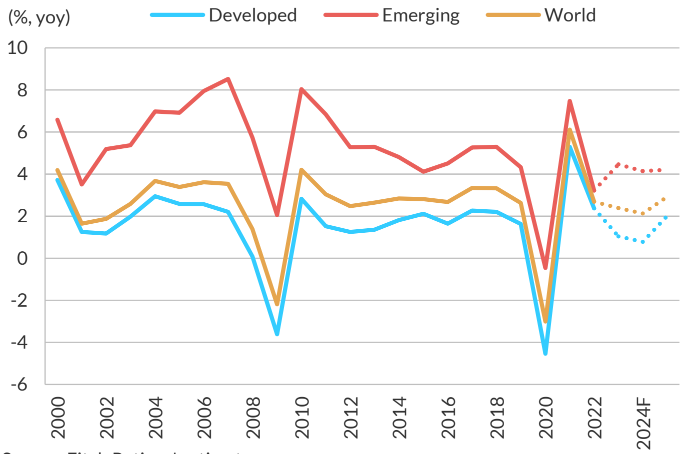

Pawel Borowski
+44 20 3530 1861
pawel.borowski@fitchratings.com

Global Forecast Summary

(%)	Annual Average 2018-2022	2022	2023F	2024F	2025F
GDP Growth					
US	2.1	2.1	1.2	0.5	2.4
Eurozone	1.2	3.5	0.8	1.4	1.7
China	5.3	3.0	5.6	4.8	4.7
Japan	-0.2	1.0	1.3	1.0	0.8
UK	0.8	4.1	-0.1	1.0	1.8
Developed [a]	1.4	2.4	1.0	0.8	2.0
Emerging [b]	4.0	3.2	4.5	4.1	4.2
Emerging ex-China	2.5	3.5	2.9	3.2	3.5
World [c]	2.3	2.7	2.4	2.1	2.9
Inflation (end of period)					
US	3.6	6.5	3.6	2.7	2.5
Eurozone	2.8	9.2	4.0	2.5	2.0
China	2.1	1.8	1.2	1.8	2.2
Japan	0.7	4.0	1.7	1.3	1.2
UK	3.4	10.5	5.0	3.0	2.5
Interest Rates (end of period)					
US	1.40	4.50	5.75	4.25	3.25
Eurozone	0.15	2.50	4.50	3.75	3.00
China [d]	3.07	2.75	2.65	2.65	2.65
Japan	-0.10	-0.10	-0.10	-0.10	-0.10
UK	0.64	3.50	5.25	4.25	3.50
US 10-Year Yield	2.05	3.88	4.25	4.00	3.75
Exchange Rates and Oil					
Oil (USD/barrel)	69.6	98.6	80.0	75.0	70.0
USDJPY (end-period)	113.5	132.7	135.0	130.0	125.0
USDEUR (end-period)	0.88	0.94	0.92	0.92	0.92
GBPUSD (end-period)	1.30	1.21	1.20	1.20	1.20
USDCNY (end-period)	6.72	6.99	7.20	7.30	7.30

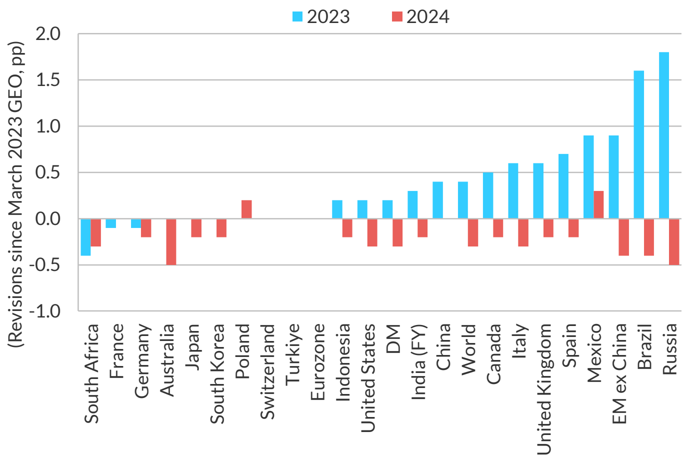
[a] US, Japan, France, Germany, Italy, Spain, UK, Canada, Australia and Switzerland
[b] Brazil, Russia, India, China, South Africa, Korea, Mexico, Indonesia, Poland and Turkiye
[c] 'Fitch 20' countries weighted by nominal GDP in US dollars at market exchange rates (three-year average)
[d] One-year medium-term lending facility
Source: Fitch Ratings

World GDP Growth



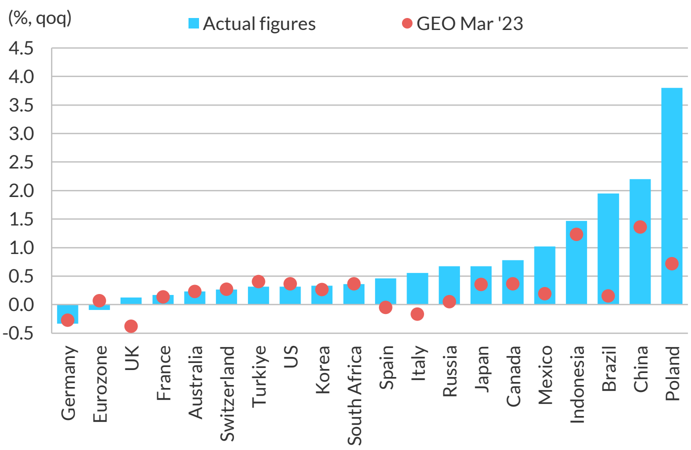
Source: Fitch Ratings' estimates

Revisions to Annual GDP Growth Forecasts



Source: Fitch Ratings

GDP 1Q23 Outturns vs Forecasts



Source: Fitch Ratings' estimates, national statistical offices, Haver Analytics

Forecast Highlights

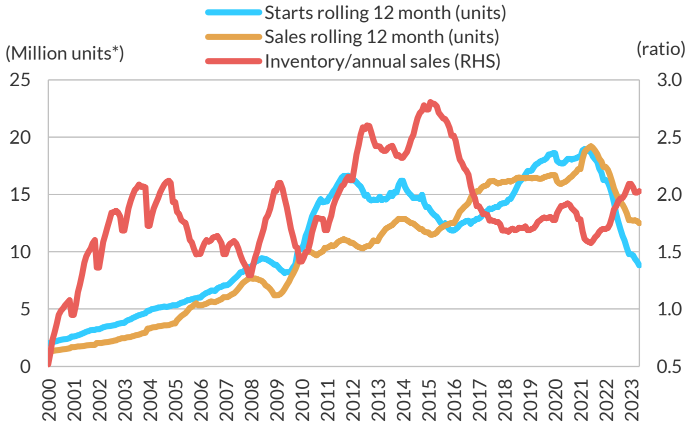
Near-term global growth prospects have improved again as consumption and job creation in the US prove surprisingly resilient, China's reopening prompts a swift rebound in services activity and the expansion in EM ex-China outperforms expectations. We now forecast world growth at 2.4% in 2023, revised up by 0.4pp. This would, however, still represent a slowdown from the 2.7% outturn in 2022. Moreover, we now expect global growth to slow further in 2024 to 2.1%, revised down from 2.4% in the March GEO. The downward revision to 2024 partly reflects more challenging base effects for EM growth after stronger recoveries in China and elsewhere this year. But it also embodies a view that monetary policy tightening in the US and Europe is taking longer than anticipated to take its toll fully on aggregate demand.

In this context, we are now looking at a more protracted, two-year period during which world activity will be depressed by monetary policy tightening. This is illustrated in our developed country aggregate growth forecasts, at 1.0% this year and 0.8% next. These are well below trend and embody recessions in the US and UK. For 2025, included in the GEO forecast horizon for the first time, we expect developed market growth to pick up to 2%, partly reflecting the delayed impact of interest rate cuts in 2024.

Upward revisions to 2023 growth forecasts have been most pronounced for EM. GDP outturns in 1Q23 proved a lot stronger than expected in China, Brazil, Russia, India and Mexico, and all have seen marked increases in annual growth forecasts. China's abrupt removal of pandemic restrictions saw a larger-than-expected jump in activity across the board in 1Q23. Monthly indicators – particularly property and exports – have weakened more recently, but the normalisation of consumption from heavily constrained levels in 2022 is continuing as unemployment falls and household confidence slowly recovers. The Chinese authorities have also started to ease policy more assertively and we anticipate cuts in banks' reserve requirement ratios. Even with slower momentum through the rest of this year, annual GDP growth of 5.6% now looks achievable. A recovery in the property sector remains elusive, but some signs of stabilisation are starting to emerge and the overhang of completed but unsold housing inventory looks smaller now than in 2015

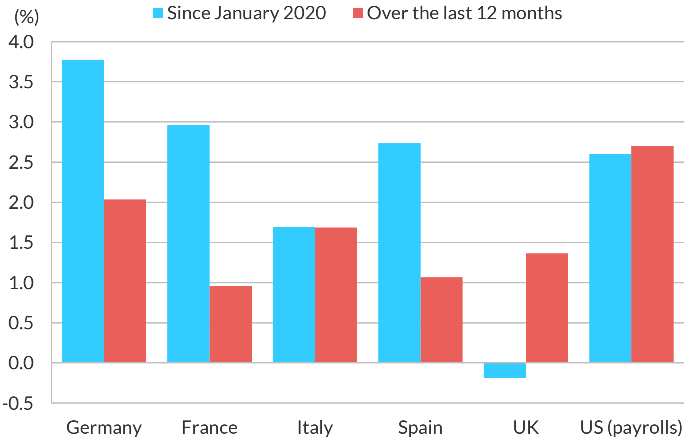
Brazil's economy expanded very sharply in 1Q23 helped by a bumper harvest and with domestic demand supported by a strong labour market and fiscal easing. This pace is unlikely to be sustained but we have revised 2023 growth up to 2.3% from 0.7% in the March GEO. India's economy has been showing broad-based strength – with GDP up by 6.1% year on year (yoy) in 1Q23 and auto sales, PMI surveys and credit growth remaining robust in recent months – and we have raised our forecast for the fiscal year ending in March 2024 (FY23-24) by 0.3pp to 6.3%. In Mexico, tight labour markets, buoyant consumer confidence and strong remittance flows are supporting the economy and with a Banxico policy rate cut expected later this year, we have upgraded the 2023 forecast to 2.5%. Russia's economy now looks likely to record moderate growth this year. The yoy decline in GDP in 1Q23 was far shallower than expected, business and consumer surveys have been improving and credit growth has started to recover.

China - Housing Starts, Sales and Inventory



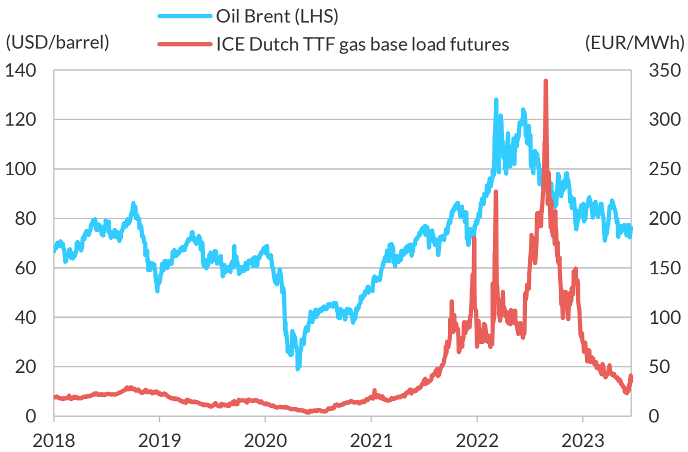
*assuming 900 sq m per unit
Source: Fitch Ratings, NBS, Haver Analytics

Employment Growth



Source: Fitch Ratings, FSO, Eurostat, ISTAT, ONS, BLS, Haver Analytics

Global Oil Price and EU Wholesale Natural Gas Price



Source: Fitch Ratings, Financial Times, Intercontinental Exchange, Haver Analytics

Our previous forecast of a US recession commencing in 3Q23 now looks premature as momentum in job growth and consumer spending has remained robust well into 2Q23. Nevertheless, we still expect tighter credit conditions, weakening business investment, upward pressure on the savings ratio and slowing exports to result in quarterly contractions in 4Q23 and 1Q24. UK economic growth remained marginally positive in 1Q23 but we expect a recession to commence in 2Q23 as higher mortgage interest rates start to weigh on households' debt service. UK GDP is still expected to decline on an annual basis in 2023 – unique among the Fitch 20 – but by less than we expected in March.

Our eurozone aggregate GDP forecasts are unchanged, as a further easing in the natural gas crisis is broadly offset by more aggressive monetary policy tightening. The single-currency area suffered a mild recession in 4Q22 and 1Q23 as the terms-of-trade shock weighed on real incomes and disrupted industrial production, particularly in Germany. But employment has held up and growth in Italy and Spain has been surprisingly resilient. Both stand to benefit from stepped up NextGeneration EU (NGEU) investment and the recovery in international tourism.

Sources of Global Growth Resilience

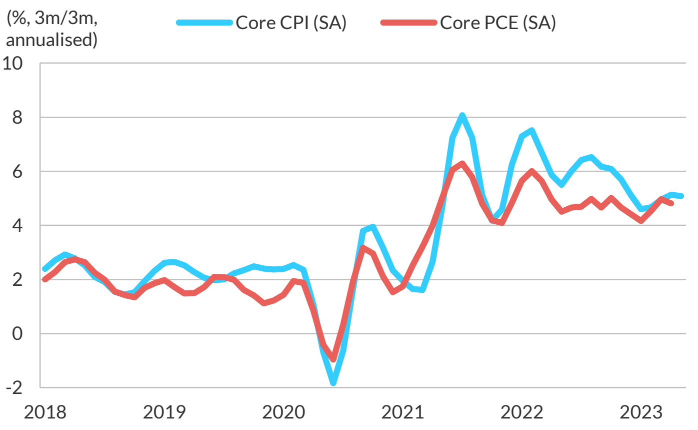
Several factors help to explain the notable resilience of global growth so far in 2023. One is the strength of labour markets. Unemployment rates have remained very low by historical standards in the US and Europe, enhancing job security and household confidence. Employment has grown by around 1.5% in the eurozone and UK in the past 12 months, and, on the payrolls measure, by 2.7% in the US. This has supported aggregate household sector real income growth, helping to counter the effect of higher inflation on real income per household.

Exceptional savings buffers accumulated through the pandemic also have been a factor. US households have been spending a higher share of their monthly income – relative to pre-pandemic historical norms – since the start of 2022. We believe this has been helped by the drawdown of the cushion of 'excess savings' that was built up in 2020 and 2021 when government transfers and artificially suppressed consumption levels saw savings surge to record highs.

Easing supply constraints also likely supported activity in early 2023. Global manufacturing supply-chain bottlenecks started to ease in late 2022 and this accelerated in early 2023. Reduced input shortages recently have helped autos production, and the resilience of US durable goods consumption could partly reflect delayed orders finally being fulfilled. The sharp fall in European wholesale gas prices has also supported real incomes and activity in Europe in the past few months. We have lowered our EU natural gas price assumption to EUR39/MWh (2023 annual average) from EUR68/MWh in the March GEO. Oil prices have also been falling and we have revised down our 2023 oil price assumption to USD80 a barrel (bbl) for Brent crude oil from USD85/bbl before.

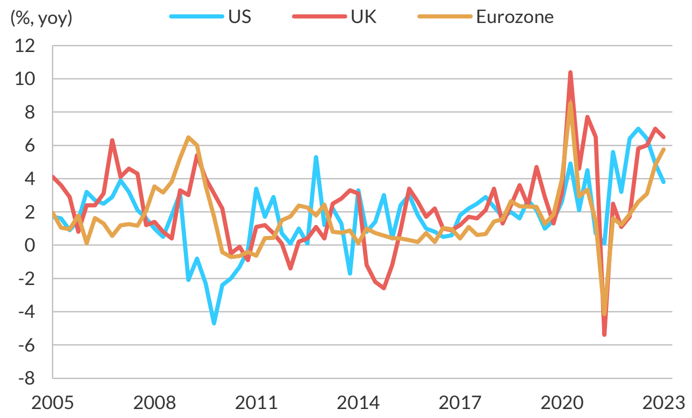
We do not expect these factors to continue to support growth for much longer. Employment is typically a lagging indicator of the wider economic developments in Europe, and recent US payrolls strength looks somewhat at odds with the decline in job openings, falling average weekly hours and rising weekly unemployment benefit clams. Our analysis suggests that the cushion of excess household savings in the US has fallen by 60% and that a substantial portion of the remainder is unlikely to be spent as it has accrued to

US Core Inflation Momentum



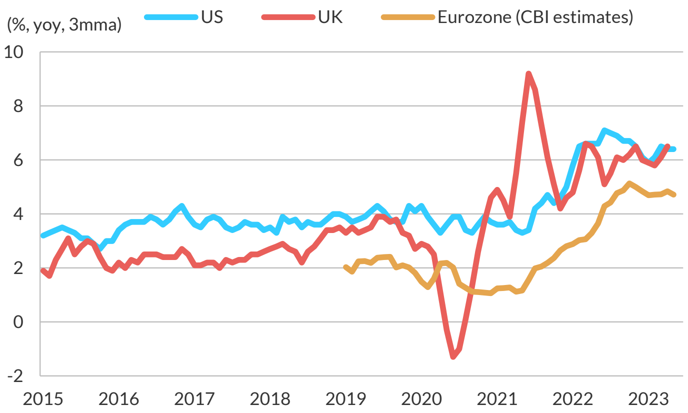
Source: Fitch Ratings, BLS, BEA, Haver Analytics

Unit Labour Costs



Note: Data for UK for 3Q22 onwards are Fitch's estimates
Source: Fitch Ratings, BLS, Eurostat, ONS, Haver Analytics

Nominal Wage Growth Measures



Source: Fitch Ratings, Atlanta Fed, ONS, Central Bank of Ireland, Haver Analytics

high-income households. The global manufacturing cycle is also cooling rapidly as world trade slows. World trade in goods and services is expected to slow to 1.5% in 2023 from 5.6% in 2022.

However, another factor at play here is the continued strength of nominal GDP growth. US nominal GDP – which broadly corresponds to total dollar income received by all households and firms in the economy – grew 7.1% yoy in 1Q23, much faster than the 1.6% expansion in real output. The 5.3% rise in the GDP deflator partly reflects the fact that firms have, by and large, been able to pass on higher costs to consumers, with little evidence of a sharp squeeze in profits to date. Workers have also been able to resist some of the shock to real incomes from higher inflation by bidding up nominal wages. But while strong nominal income growth may be helping to sustain demand, it is also a sign of inflation becoming entrenched, as labour costs and profits per unit of real output rise.

Core Inflation Is Proving Sticky

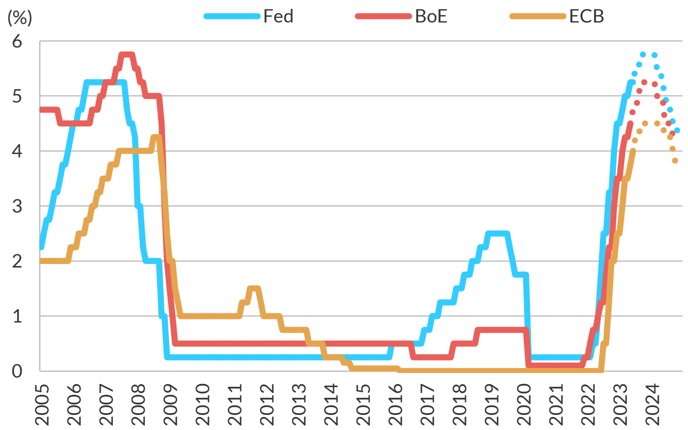
This speaks to the problem of sticky core inflation. Headline inflation has fallen significantly in the US and Europe since late 2022, but there has been precious little progress in bringing down core inflation (i.e. CPI excluding food and energy). US core inflation momentum (on a three-month-on-three-month annualised basis) has been at around 5% for the past six months. Eurozone core inflation is similarly stuck at more than 5% yoy and core inflation in the UK is still rising, recently exceeding 7% yoy. This intransigence is despite easing global supply-chain pressures helping to slow core goods inflation and reflects accelerating services prices. Some of the latter can be explained by reopening effects but a key driver of inflation in services – a labour-intensive sector – is rising labour costs. Rising nominal wage inflation, allied with weak productivity growth, has resulted in a sharp rise in unit labour costs (ULC), which rose by more than 6% last year in the US – the highest rate since the early 1980s. ULC growth recently reached similar levels in the eurozone and UK. This is clear evidence of inflation pressures becoming self-reinforcing as higher prices lead to higher wages, in turn pushing up firms' costs. Tight labour markets increase the risk of wage and price inflation persistence which would, in the absence of a policy response, keep inflation well above target.

Policy Rates Higher for Longer

It is against this backdrop that comments by central bankers have taken a renewed hawkish turn in recent months. The failure of core inflation to respond to aggressive rate rises since mid-2022 has become a key concern. Central banks have gleaned little comfort from recent falls in headline inflation as this partly reflects developments in global energy markets, which are beyond their control. Moreover, food price inflation has been hard to forecast, proving a lot more persistent than expected in recent months given earlier falls in global agricultural commodity prices. Recent hawkish commentary from the Fed, ECB and BOE has placed heavy emphasis on the role of high wage inflation and rapid ULC growth in keeping core inflation high. Concerns are amplified by low unemployment and ongoing labour market imbalances, exacerbated – in the case of the US and UK – by lasting declines in labour force participation rates.

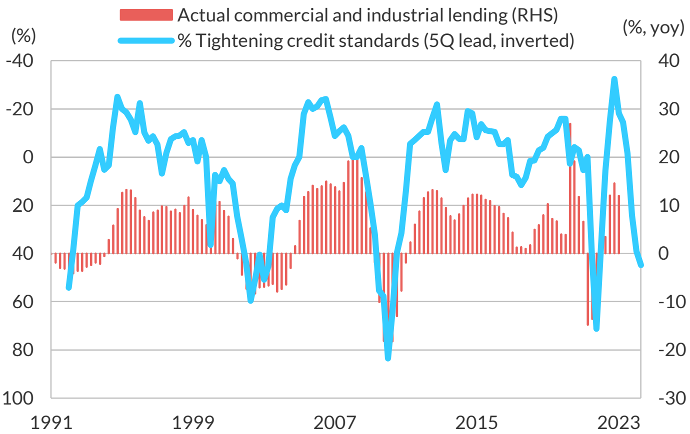
The Fed slowed the pace of rate increases to 25bp at its February, March and May meetings and held rates in June for the first time since January 2022. But while this profile suggests the Fed believes

Policy Interest Rates Outlook - US, UK and Eurozone



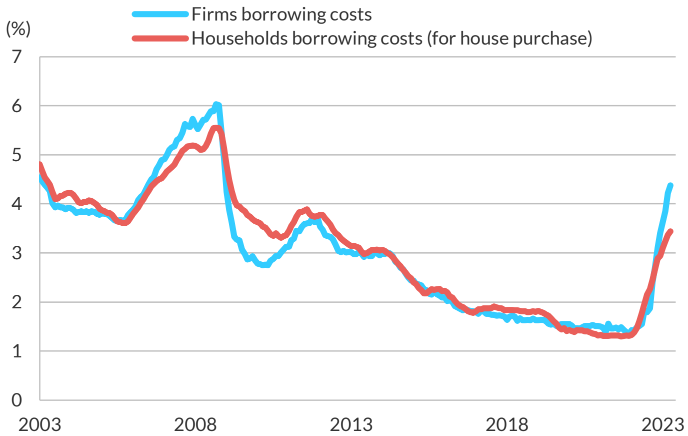
Source: Fitch Ratings' estimates, Fed, ECB, BoE, Haver Analytics

US Senior Loan Officer Survey and Lending to Firms



Source: Fitch Ratings, Fed, Haver Analytics

Eurozone Bank Lending Rates



Source: Fitch Ratings, ECB, Haver Analytics

that a rate peak is getting close, it signalled at the June meeting that further increases will be required. We now expect two more 25bp hikes in July and September, taking the federal funds (upper) rate to 5.75%. The ECB raised rates by 25bp in June and said that a further increase is very likely in July. We believe the ECB will go further and also raise rates again in September, taking the MRO to 4.5%. We expect the BOE to raise rates three more times to 5.25%.

With further rate rises also now expected in Australia, Canada and Switzerland, end-2023 interest rate forecasts have been revised up for all of the Fitch10 developed economies, except Japan. Compared to March, end-2023 policy rate projections have been revised up by 25bp for the US and Switzerland, 50bp for the ECB, BOE and Bank of Canada (BOC) and 75bp for the Reserve Bank of Australia (RBA). The picture in emerging markets is much more mixed, with rate projections revised down for Brazil, Mexico, India, Indonesia and China. The Fed and ECB are not expected to start cutting rates until March and June 2024, respectively, leaving end-2024 rates above our March projections.

Long and Variable Lags

The rapid pace of interest rate rises since the middle of last year in the US and Europe has had a smaller impact on the economy than many expected. But economic history suggests 'long and variable lags' in the transmission of monetary policy, with 18-24 months typically seen as a sensible guide. Moreover, the rate rises began from an extremely low starting point. Policy rates only moved above estimates of 'neutral' – based on estimated equilibrium real rates plus inflation targets – at the end of 2022. Real policy interest rates – calculated on a backward-looking basis using average core inflation over the past three months – only recently turned positive in the US, and they remain negative in the UK and eurozone. Pandemic savings buffers may have delayed the substitution effect of higher interest rates in reducing consumption. The preponderance of long-term fixed-rate mortgages in the US has also dampened the adverse impact of rate rises on household debt-service burdens. The effective interest rate on outstanding US home mortgage debt has only moved up marginally, as has the aggregate mortgage debt-service ratio.

Nevertheless, there is ample evidence that the channels of monetary policy are working. Policy hikes have been passed onto new borrowing rates faced by firms and households. Notably, new mortgage affordability has deteriorated at a record pace in the US, in turn sharply reducing demand for new housing. Lead indicators of business investment have also weakened significantly. More broadly there has been a sharp deterioration in banks' willingness to lend as reflected in Senior Loan Officer Opinion Surveys. The asset price channel has been seen in widespread corrections in house prices. With rate hikes already causing disruptions in parts of the financial sector, there is no reason to believe economies have become immune.

Risks of Sharper Credit Tightening

The immediate impact of recent US banking sector stresses on credit supply has been limited. But banks' funding costs are rising and with QT reducing banking system reserves and putting downward pressure on deposits, there is a risk that credit conditions may tighten more rapidly than anticipated.

United States

Consumer spending and employment are holding up better than expected but evidence of slowing demand continues to accumulate. We expect the Fed to raise rates by 25bp in July and September and we expect a recession in 4Q23 and 1Q24 with a peak-to-trough decline in real GDP of 1.1%.

GDP grew by 0.3% (or 1.3% annualised) in 1Q23. This was slightly weaker than expected in our previous GEO but the details showed surprisingly fast consumer spending growth at 0.9%, offset by a large drag from slower inventory accumulation. Consumer spending continued to grow in April and payrolls increased by an average of 320,000 in April and in May.

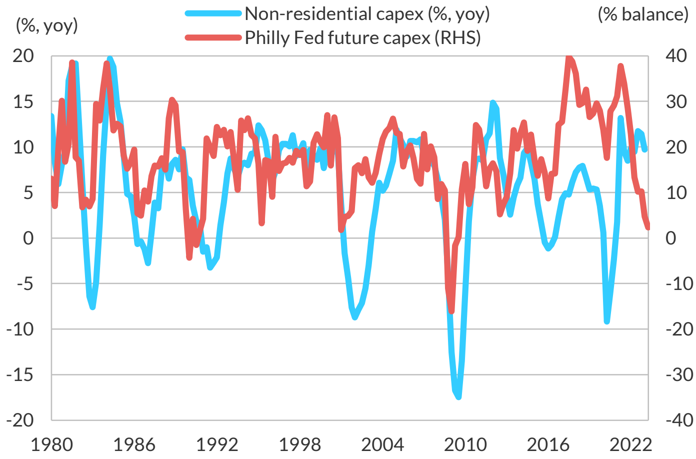
Nevertheless, there is increasing evidence that the slowdown in demand is broadening. Lead indicators of business investment have deteriorated in recent months, manufacturing output is stagnant and manufacturing PMI surveys have fallen well below 50, the level that indicates growth or contraction. Alternative indicators of labour demand – including average weekly hours worked and job openings – have weakened, and unemployment benefit claims have edged up.

There is no evidence of an immediate credit crunch in the aftermath of banking sector stresses in March, but rising bank funding costs are likely to intensify the tightening in credit conditions that was already underway in response to aggressive Fed tightening. A cushion of excess savings accumulated during the pandemic in 2020 and 2021 has helped to support consumption in the past year or so but these buffers have now been drawn down by 60% and are unlikely to go on supporting consumption beyond this year.

That said, the impact of monetary tightening on jobs and spending is taking longer to unfold and we now expect the economy continuing to expand in 2Q23 and 3Q23. We still see a recession ahead, driven by tighter credit conditions, upward pressure on the savings ratio, weakening business investment and a slowdown in exports. Job growth is also expected to turn negative later this year. But the recession is now expected to start a little later in 4Q23.

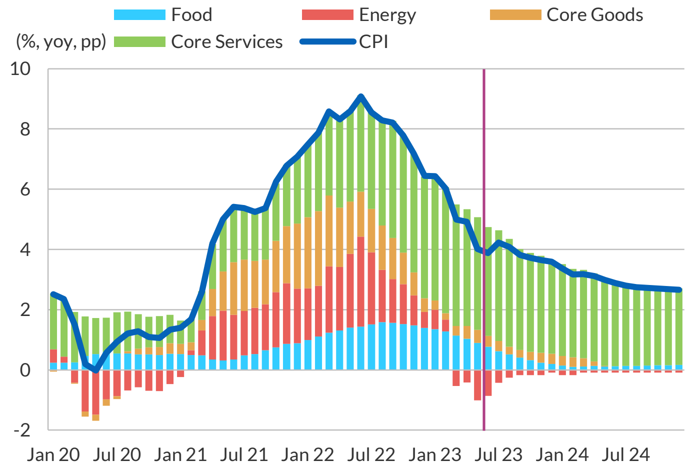
The Fed raised interest rates by 25bp in March and May and despite the pause in June, we expect two further rises to 5.75% by September. Core inflation remained stubbornly high at 5.3% yoy in May and we only expect it to fall to 4.5% by year-end. This will likely preclude any cuts in the federal funds rate until March 2024.

US - Business Investment and Philadelphia Fed Survey



Source: Fitch Ratings, Philadelphia Fed, BEA, Haver Analytics

US - CPI Inflation and Contributions



Source: Fitch Ratings' calculations, BLS, Haver Analytics

United States - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	2.1	2.1	1.2	0.5	2.4
Consumer spending	2.6	2.7	1.8	0.2	2.4
Fixed investment	2.5	-0.2	-1.8	-0.1	2.6
Net trade (contribution pp)	-0.6	-0.6	0.3	-0.1	-0.3
CPI inflation (end-year)	3.6	6.5	3.6	2.7	2.5
Unemployment rate	4.9	3.6	4.0	5.1	4.5
Policy interest rate (end-year)	1.40	4.50	5.75	4.25	3.25
Exchange rate, USDEUR (end-year)	0.88	0.94	0.92	0.92	0.92

Source: Fitch Ratings

Eurozone

We have not changed our eurozone growth forecasts, while introducing a new forecast for 2025. Upgrades to Spain and Italy are balanced by a slightly weaker outlook for Germany. The eurozone economy contracted by 0.1% quarter on quarter (qoq) in 1Q23, slightly below our expectation for 0.1% growth in the March GEO. This was partly a product of volatility in Irish GDP. Growth for Germany, France, Italy and Spain, upon which we base our forecast, and which together make up 70% of eurozone output, was 0.1%.

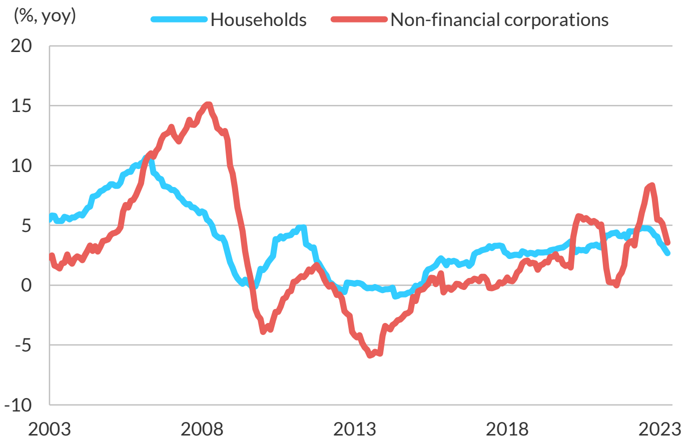
Consumption fell for a second successive quarter but will , we think, recover as price pressures ease. On the supply side, global manufacturing weakness is weighing on the prospects of Europe's manufacturing sector, even as firms continue to benefit from large order books and supply chain problems fade. Forward-looking measures, such as demand for credit, point to lower investment ahead. Higher interest rates will weigh on demand to a greater extent even as lower inflation supports real incomes.

Inflation has fallen slightly faster than we expected in March, to 6.1% in May. Energy price inflation, which contributed 4.3pp to the peak headline inflation rate of 10.6% in October 2022, has now turned negative, but core inflation is barely lower at 5.4%. We have slightly lowered our CPI forecast. Risks to the forecast include renewed energy and food price shocks; natural gas futures prices for winter 2023-2024 have recently steepened although spot prices are back to 2021 averages.

The ECB raised its policy rates by 25bp at the June 15 meeting, and said it would make a further 25bp rise in July barring a sudden change in conditions. The accompanying messaging – including concerns over unit labour costs and the potential for persistence in core inflation – makes it more likely that the ECB will continue to hike, probably in September, by 25bp. We forecast two more hikes, taking the deposit rate to 4.0% and the main refinancing operations (MRO) rate to 4.5%. The ECB confirmed that it would accelerate the pace of balance sheet runoff as trailed at the May meeting, a slightly faster pace than we had expected.

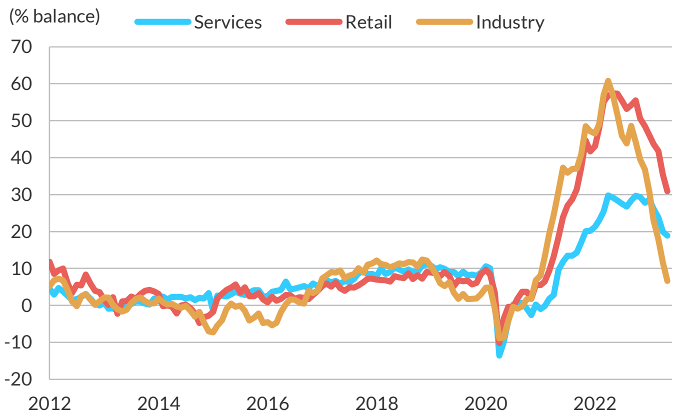
We have also lowered our forecasts for eurozone unemployment; a forecast change mirrored by the ECB in its June projections. Job creation has outpaced growth in terms of annualised rates, and payrolls have grown throughout the 'technical recession' in GDP during the winter.

Eurozone - Bank Lending



Source: Fitch Ratings, ECB, Haver Analytics

Eurozone - Selling Price Expectations



Note: Balance of respondents expecting prices to rise
Source: Fitch Ratings, European Commission, Haver Analytics

Eurozone - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	1.2	3.5	0.8	1.4	1.7
Consumer spending	0.7	4.5	0.3	1.4	1.8
Fixed investment	2.3	3.7	0.9	2.3	2.7
Net trade (contribution pp)	0.0	-0.2	0.8	0.1	0.1
CPI inflation (end-year)	2.8	9.2	4.0	2.5	2.0
Unemployment rate	7.6	6.7	6.8	6.8	6.5
Policy interest rate (end-year)	0.15	2.50	4.50	3.75	3.00
Exchange rate, EURUSD (end-year)	1.14	1.07	1.09	1.09	1.09

Source: Fitch Ratings

China

China's reopening rebound was a lot stronger in 1Q23 than we had anticipated but activity indicators have slowed more recently and we have only revised up our annual 2023 GDP forecast modestly to 5.6%, from 5.2% in the March GEO.

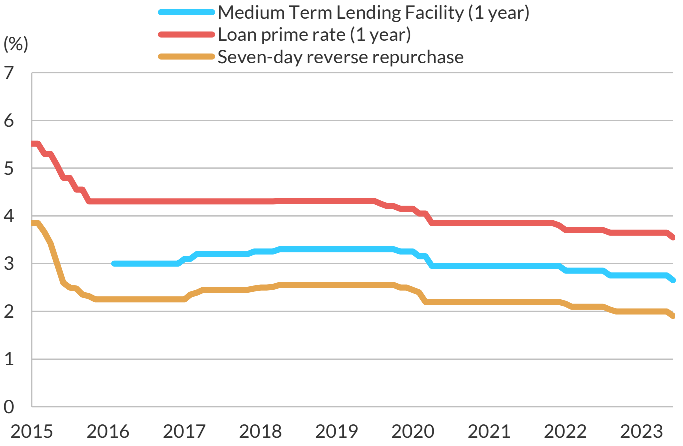
GDP expanded by 4.5% yoy in 1Q23 compared to an estimate of 2.8% in the March GEO and by 2.2% qoq (compared to 1.4% in March). Consumption, property sales and exports all recovered rapidly in February and March after the swift removal of pandemic mobility restrictions which had severely disrupted activity and spending in 4Q22. However monthly macro data releases for April and May slowed markedly. Fixed asset investment growth slowed to 1.9% yoy in May (from 4.7% in March), industrial production slowed to 3.5% (from 3.9% in March), credit growth slowed by 0.5pp to 9.3% yoy and exports fell by 7.5% yoy. Property sales and starts saw a sharp renewed deterioration, falling by 16% and 30% yoy, respectively, in May.

Nevertheless, the broader picture of a growth recovery driven by a normalisation of consumer spending – from levels that were heavily supressed by pandemic restrictions in 2022 – looks intact. Retail sales continued to expand robustly in May, PMI services balances remained well above 50 and consumer confidence surveys have started to recover after diving to record lows in 2022. Industrial production growth also recovered on a month-on-month (mom) basis in May.

Moreover, household income prospects should continue to improve as labour demand recovers and the unemployment rate falls. And while a property-sector recovery remains elusive, there are some signs of stabilisation. Housing completions have picked up sharply suggesting that work on stalled projects has resumed. This matters for restoring buyer confidence given the dominance of pre-sales in the market for new housing. Our estimates of completed but unsold new housing units – based on the cumulative gap between starts and sales since 2000 – also suggest that the inventory overhang as a share of sales is significantly lower now than in 2015.

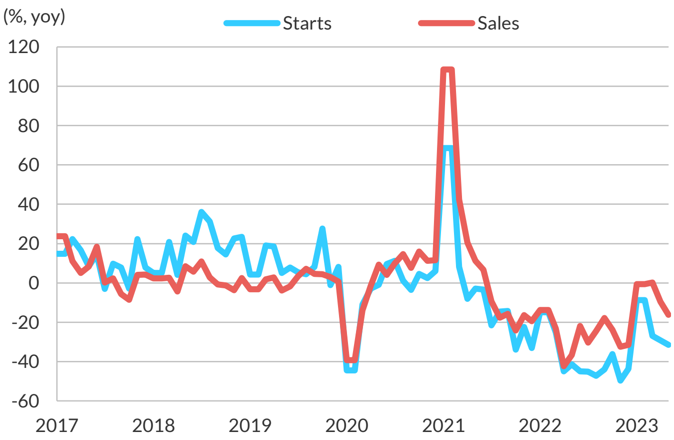
The authorities' willingness to provide some macro policy stimulus to support growth also looks to be increasing. The PBOC cut the seven-day reverse repo rate and the one-year MLF and LPR policy lending rates by 10bp in June. Further cuts in banks' reserve requirement ratios also look likely after the recent dip in credit growth. With consumption recovering and the drag from falling construction activity easing, domestic demand growth will pick up in 2023. This should more than offset a rising drag from net trade as exports weaken and services imports rise.

China - Interest Rates



Source: Fitch Ratings, PBOC, Haver Analytics

China - Housing Starts and Sales



Source: Fitch Ratings, CNBS, Haver Analytics

China - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	5.3	3.0	5.6	4.8	4.7
Consumer spending	4.9	0.1	8.7	6.1	3.2
Fixed investment	4.4	3.1	4.6	4.6	5.2
Net trade (contribution pp)	0.8	0.7	-0.3	-0.3	0.3
CPI inflation (end-year)	2.1	1.8	1.2	1.8	2.2
Policy interest rate (end-year)	3.07	2.75	2.65	2.65	2.65
Exchange rate, USDCNY (end-year)	6.72	6.99	7.20	7.30	7.30

Source: Fitch Ratings

Japan

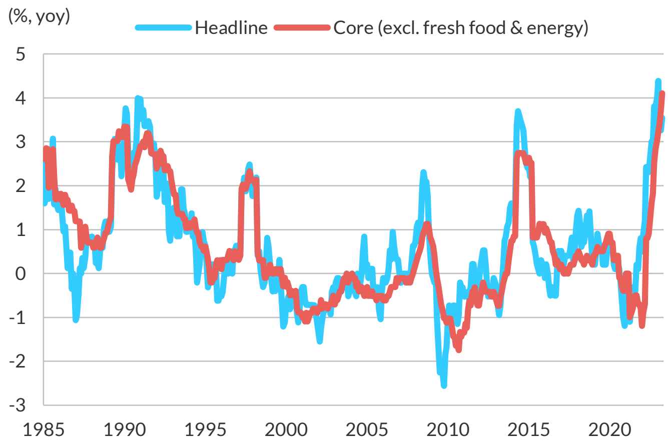
The 0.7% qoq GDP expansion in 1Q23 was stronger than we had expected in March's GEO, as solid growth in consumer spending and investment more than offset a negative contribution from net trade. Industrial production and retail turnover both fell in April, but capital goods shipments rose and the May business surveys also pointed to the positive momentum continuing into 2Q23.

However, the pace of growth is set to slow sharply. The rapid drop in the household savings rate in 1Q23 back to its pre-pandemic level suggests that consumers have less scope to dip into their savings to maintain their spending. Meanwhile, the slowdown in global trade that we expect this year is likely to weigh on exports. Against that backdrop, weaker business investment also seems likely, which is supported by the recent weak momentum in machinery orders. We expect overall GDP growth of 1.3% this year. With the negative output gap nearly closed, we expect the pace of growth in 2024 and 2025 to slow, to 1% and 0.8%, respectively.

Headline inflation has dropped sharply as government energy subsidies have taken effect. But the government has approved tariff increases this summer by regional electricity companies. More significantly, core inflation (excluding fresh food and energy) has continued to climb, exceeding 4% in April for the first time in more than 40 years, and looks set to remain very high by Japanese standards. Surveys show firms' selling price expectations continue to rise, while a large majority of consumers expect inflation to still be above 2% in a year's time.

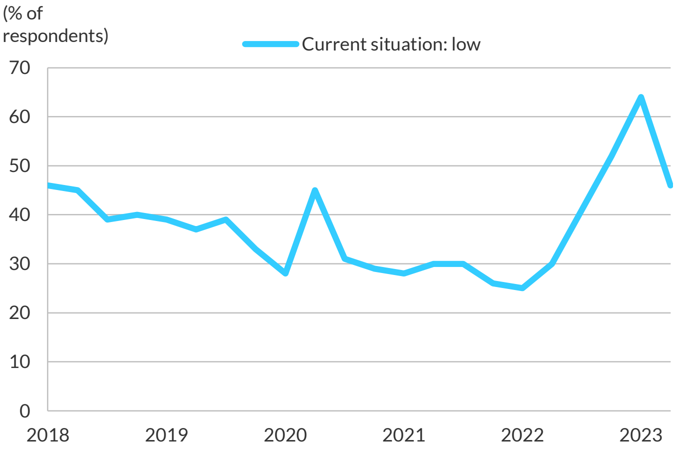
Although inflation now appears to have taken hold for the first time in decades, the Bank of Japan (BOJ) has stuck resolutely to its ultra-accommodative policy stance. There has been little signal from the new BOJ Governor Kazuo Ueda that this is about to change soon. We therefore continue to expect the policy rate to remain at -0.1% through 2025. Since the BOJ is undertaking a policy review that is scheduled to last 12-18 months, we also now expect there to be less chance that there will be further imminent adjustments to the yield curve control policy. Nevertheless, given the continued poor functioning of the JGB market, we think that yield curve control will have to be substantially altered at some point in the next year.

Japan - Headline CPI and Core Inflation



Source: Fitch Ratings, MIC, Haver Analytics

Japan - Survey of Bond Market Functioning



Source: Fitch Ratings, Bank of Japan, Haver Analytics

Japan - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	-0.2	1.0	1.3	1.0	0.8
Consumer spending	-0.5	2.0	1.4	0.8	0.7
Fixed investment	-0.7	-1.0	2.2	1.2	1.0
Net trade (contribution pp)	-0.2	-0.5	-0.3	0.1	0.1
CPI inflation (end-year)	0.7	4.0	1.7	1.3	1.2
Unemployment rate	2.6	2.6	2.7	2.7	2.6
Policy interest rate (end-year)	-0.10	-0.10	-0.10	-0.10	-0.10
Exchange rate, USDJPY (end-year)	113.5	132.7	135.0	130.0	125.0

Source: Fitch Ratings

United Kingdom

The UK economy has proved resilient to higher interest rates and the hit to real incomes so far this year. The 0.1% expansion in GDP in 1Q23 was stronger than we had forecast in March, and the monthly data for April suggest that this continued at the start of 2Q23. The larger fall in energy prices, alongside strong nominal incomes growth and some protection from the shift to fixed interest rate products, have all helped support economic activity even as the BOE has raised rates.

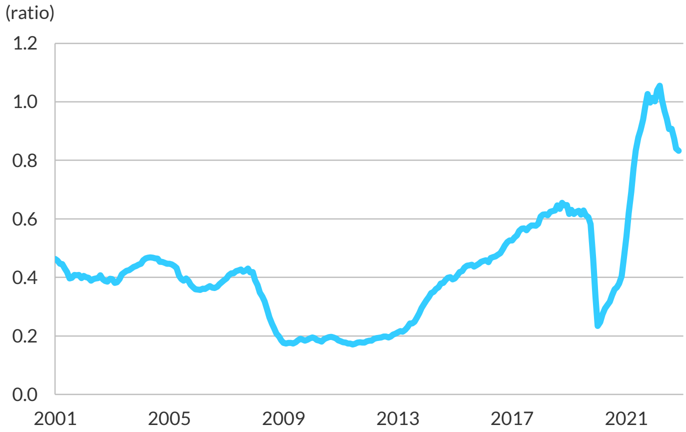
But we still think a recession is highly likely this year. Despite recently exceeding expectations, underlying momentum in the economy was still weak over the past 9-12 months. The impact of the BOE's most aggressive tightening cycle since it gained independence will soon start to be felt more acutely; indebted households are likely to see a jump in interest payments this year. UK mortgage rates have recently increased as markets have come to anticipate ongoing rate increases from the BOE. Many two-year fixed-rate mortgages taken out in 2021 will see rates reset upwards in 2023.

Headline inflation is subsiding and will continue to do so as base effects related to energy and food drop out of the annual rate, and falls in wholesale commodity prices eventually feed through to consumer prices. This will help to limit the scale of the recession – we expect the peak-to-trough fall in GDP to be in the region of 0.5% and GDP to shrink by just 0.1% in 2023. With much of the past tightening yet to be felt, GDP growth is likely to be fairly anaemic at 1.0% in 2024, before a recovery in 2025.

However, core inflation and wage pressures have been much stickier than the BOE was expecting. In particular, services inflation is likely to remain elevated as the tightness of the labour market adds to wage persistence. Private-sector regular wage growth accelerated to 7.6% in the three months to April. Overall, we have raised our end-2023 headline CPI forecast to 5.0%, with core inflation at 6%.

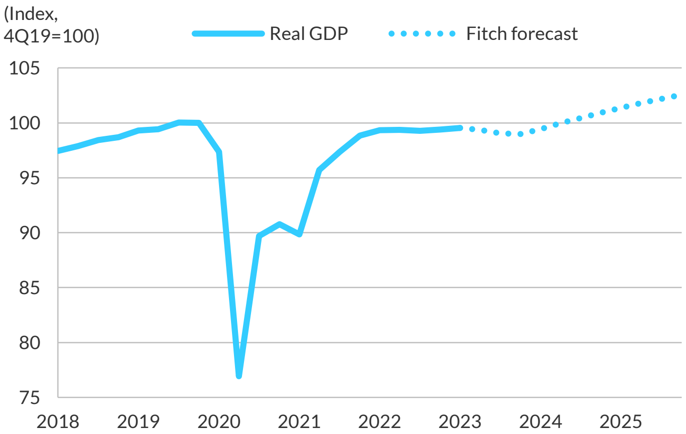
We had long thought that Bank Rate would need to rise to 4.75% to dampen inflationary pressures. But the economy's resilience and the stubbornness of core inflation means that we now think the MPC will need to go considerably further. We now expect Bank Rate to peak at 5.25% and to remain there into early 2024.

UK - Job Vacancies-to-Unemployment Ratio



Source: Fitch Ratings, ONS, Haver Analytics

UK - Real GDP



Source: Fitch Ratings' calculations, ONS, Haver Analytics

United Kingdom - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	0.8	4.1	-0.1	1.0	1.8
Consumer spending	0.4	5.6	-0.1	1.0	1.8
Fixed investment	1.2	8.6	0.2	0.1	2.0
Net trade (contribution pp)	-0.3	-1.2	1.7	0.0	0.1
CPI inflation (end-year)	3.4	10.5	5.0	3.0	2.5
Unemployment rate	4.1	3.7	4.6	4.6	4.0
Policy interest rate (end-year)	0.64	3.50	5.25	4.25	3.50
Exchange rate, GBPUSD (end-year)	1.30	1.21	1.20	1.20	1.20

Source: Fitch Ratings

Germany

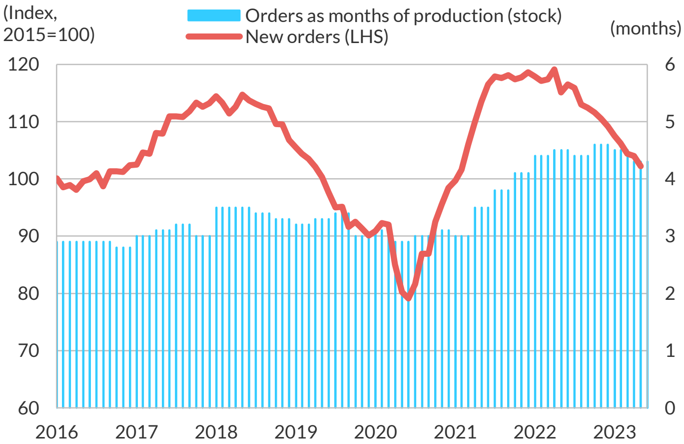
Germany recorded a 0.3% fall in GDP in 1Q23, in line with the March GEO. This marked a second successive quarter of contraction, although the economy was not in a typical recession given ongoing growth in employment. A second steep fall in consumption mainly reflected the impact of higher energy prices. Real consumption remains 3% below its 4Q19 level, compared with a shortfall of less than 1% for the eurozone as a whole. Investment recovered the 4Q22 decline in 1Q23 and net trade contributed positively, largely due to a decline in imports. The recession took the economy below its pre-pandemic level, lagging well behind post-pandemic recovery paths in France and Italy.

We expect the economy to have returned to growth in 2Q23 as signalled by the Bundesbank's weekly activity index. Flash PMIs of current activity continued to strengthen in May and remained expansionary. The main challenges include a tightening in monetary policy and in credit conditions. Retail sales for April suggest that 2Q23 got off to a tepid start and even this modest revival may be short-lived as forward-looking surveys are more downbeat.

A strong backlog of orders is still supporting German manufacturing, but new orders are weakening. Production is well short of pre-pandemic levels and the energy-intensive sectors continue to struggle despite recovering somewhat from the worst of the energy price and supply shock. Energy prices have fallen back to pre-Ukraine war levels but a resurgence is a risk.

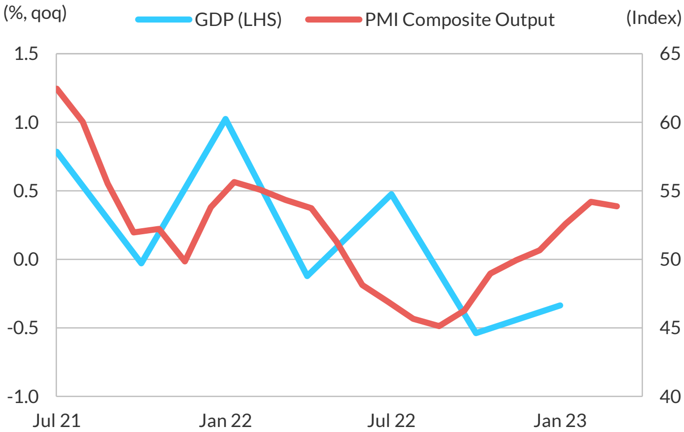
Inflation has continued to fall, with government measures including the re-introduction of a new subsidised public transport scheme accounting for part of the decline in services inflation in May. It fell to 6.3% in May, down 1.3pp from April, and core inflation subsided by 0.5pp to 5.3%. Up to 25bp of this was down to the government's introduction of a subsidised 'Germany ticket' for public transport, which reduced services price inflation. We expect a further decline during 2023.

Germany - Manufacturing Orders



Source: Fitch Ratings, Ifo, Haver Analytics

Germany - GDP and PMI Composite Output



Source: Fitch Ratings, FSO, S&P Global, Haver Analytics

Germany - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	0.6	1.8	0.0	1.2	1.6
Consumer spending	0.6	4.9	-1.6	0.8	1.5
Fixed investment	0.9	0.4	2.3	2.0	2.2
Net trade (contribution pp)	-0.5	-1.4	0.8	0.2	0.2
CPI inflation (end-year)	3.1	9.6	4.0	2.4	2.0
Unemployment rate	3.3	3.1	3.0	2.9	2.8
Policy interest rate (end-year)	0.15	2.50	4.50	3.75	3.00
Exchange rate, EURUSD (end-year)	1.14	1.07	1.09	1.09	1.09

Source: Fitch Ratings

France

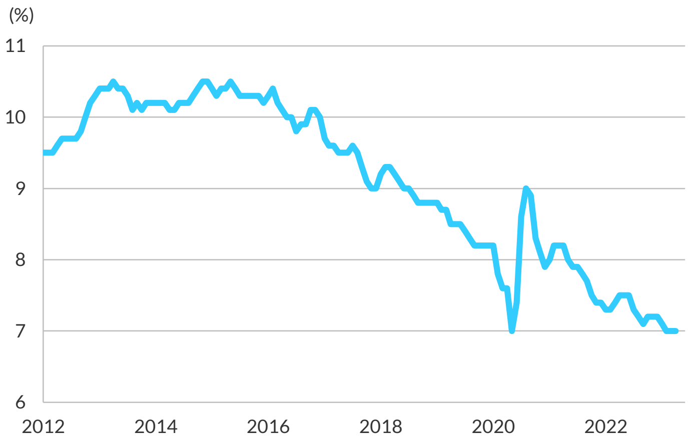
We forecast 2023 growth at 0.7% for France, barely changed from our March GEO forecast. France's economy grew just 0.2% in 1Q23 and we expect little pick-up from that pace for the remainder of the year. Consumption remains weak and will not grow notably in 2023. On the supply side, constraints are easing in manufacturing, but expectations of producers have dimmed. PMIs in the services sector point to growth, while manufacturing PMIs are contracting, as elsewhere.

The gradual recovery of purchasing power will support private consumption growth and drive firmer overall GDP growth in 2024; we have kept the growth rate at 1.3%. Extending the forecast to 2025 for the first time, we expect an acceleration in activity, helped by the impact of ECB rate cuts commencing next year. A tighter labour market notwithstanding, output remains well below where it would have been in the absence of the pandemic shock, suggesting that there is a negative output gap to be closed.

Jobs growth remained firm in 1Q23, continuing what has been a job-rich recovery from the pandemic even during the slowdown in activity in 4Q22 and 1Q23. A fall in temporary employment in 1Q23 points to a slowdown ahead. Job growth will slow even as participation continues to rise, leading to a steady or slightly rising unemployment rate in 2023. Unemployment is currently below its level prior to the pandemic.

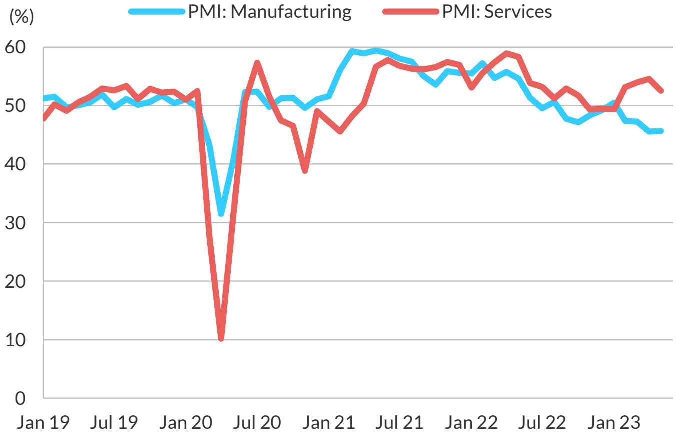
Disinflation has been much less pronounced in France so far in 2023 than in the eurozone as a whole, with HICP inflation of 6% in May. The rise in consumer energy prices was smaller than in much of the rest of the eurozone, meaning the scope for energy price deflation is lower, so the path of headline inflation is following core inflation more closely than elsewhere in the bloc. As a result, overall inflation in France is likely to be higher than the eurozone average. Expanded margins in the food sector (according to INSEE data for 1Q23) have attracted the attention of policymakers, with the economy ministry ordering supermarkets to cut food prices.

France - Unemployment Rate



Source: Fitch Ratings, Eurostat, Haver Analytics

France - PMI Surveys



Source: Fitch Ratings, S&P Global, HCOB, Haver Analytics

France - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	1.0	2.5	0.7	1.3	1.6
Consumer spending	0.7	2.3	0.2	1.2	1.9
Fixed investment	2.6	2.2	1.3	1.8	1.2
Net trade (contribution pp)	-0.3	-0.6	0.5	0.0	0.0
CPI inflation (end-year)	2.4	6.7	4.3	2.3	2.0
Unemployment rate	8.1	7.3	7.3	7.3	7.0
Policy interest rate (end-year)	0.15	2.50	4.50	3.75	3.00
Exchange rate, EURUSD (end-year)	1.14	1.07	1.09	1.09	1.09

Source: Fitch Ratings

Italy

We have made a further upgrade to our 2023 growth forecast for Italy and now expect 1.1% growth this year. The economy outperformed in 1Q23 with consumption partially recovering from a steep drop in 4Q22; it was the only one of the four large eurozone economies where consumption grew quarter on quarter. Growth is expected to be 1% in 2024.

The growth recovery from the pandemic has been boosted by investment spurred by tax breaks on residential construction and refurbishment, adding around 2% of GDP to demand since 3Q20. Housing fixed investment was still a massive 40% above 4Q19 levels in 1Q23, but housing investment is no longer growing as strongly (0.7% qoq in 1Q23) and will eventually taper off as subsidies become less generous. We expect public investment financed by the NGEU to compensate and enable overall investment to continue to grow, albeit at a much-reduced pace. Implementation delays to NGEU investment projects are a risk.

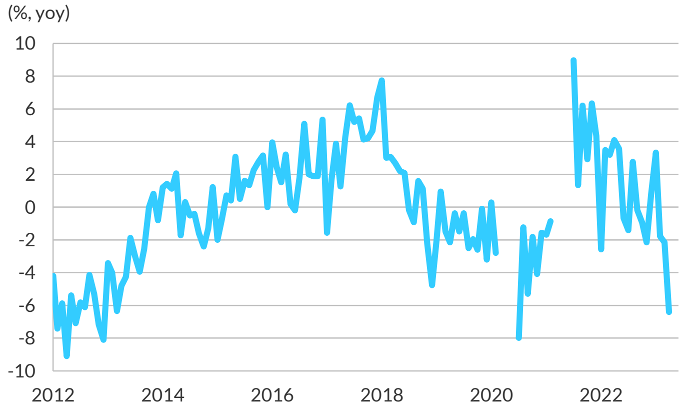
Our forecast for 2025 is for another year of above-trend growth, in view of the slack remaining in the economy and the likely support from rate cuts commencing in 2024 and stronger growth in the rest of the eurozone.

Employment has grown more quickly on an annual basis than GDP and much faster than the labour force over the past two quarters. The pace of jobs growth will slow but we expect unemployment to decline further. A rise in the participation rate is helping the labour force to grow, although the working age population continues to decline, weighing on potential GDP growth.

An unemployment rate of 8% disguises regional variations but means that Italy has one of the less tight labour markets of major eurozone countries. As such, wage pressure is lower; growth in hourly wages has been consistently below the euro area, and at 2.1% was the second-lowest among the euro area members in 1Q23, or less than half the euro-area rate. Pressure on core inflation from wage gains is therefore likely to be lower.

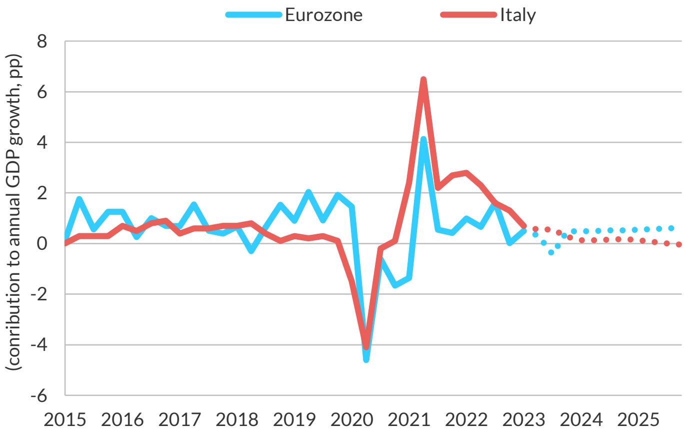
Headline inflation fell to 8.1% in May but is 2pp above the eurozone average, while core inflation was around 1pp lower. We would expect inflation to converge quickly to the eurozone average in the coming months and then head below it.

Italy - Manufacturing Output ex. Pandemic Observations



Note: Series excludes Mar-Jun 2020 and Mar-Jun 2021
Source: Fitch Ratings, ISTAT, Haver Analytics

Italy - Gross Fixed Investment



Source: Fitch Ratings, Eurostat, ISTAT, Haver Analytics

Italy - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	0.6	3.7	1.1	1.0	1.2
Consumer spending	0.0	4.6	1.3	1.1	1.6
Fixed investment	4.9	9.4	2.4	0.7	0.2
Net trade (contribution pp)	-0.2	-0.5	0.4	0.1	0.1
CPI inflation (end-year)	2.5	12.3	3.9	2.3	2.0
Unemployment rate	9.5	8.1	7.9	7.8	7.5
Policy interest rate (end-year)	0.15	2.50	4.50	3.75	3.00
Exchange rate, EURUSD (end-year)	1.14	1.07	1.09	1.09	1.09

Source: Fitch Ratings

Spain

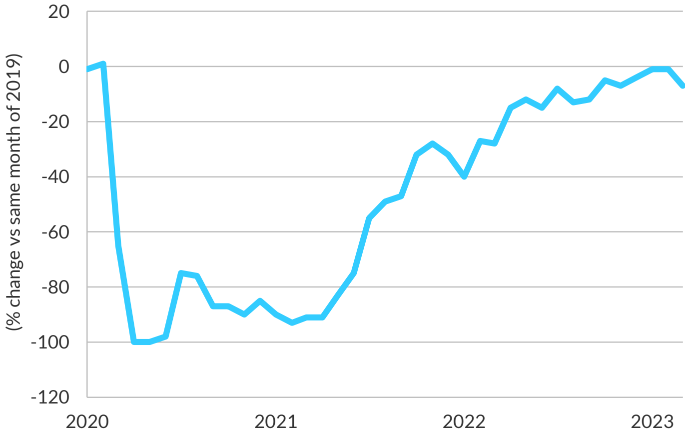
We have raised our 2023 growth forecast for Spain by 0.7pp to 1.9%, while lowering 2024 growth by 0.2pp to 1.6%. The economy performed better than expected in 1Q23 and INE revised 2022 GDP data, adding to the carryover to 2023 growth. Consumption growth unusually diverged from GDP growth in 1Q23. Consumption fell but overall activity still grew, boosted by net trade including tourism. Tourist spending rose 22% yoy in value terms in April. Spain recovered its pre-pandemic level of output in 1Q23, although consumption remains 5% short of its pre-pandemic level.

The impact from tighter financial conditions will increasingly weigh on the economic outlook. Banks report that households have reportedly responded to higher interest rates by increasing mortgage debt pre-payments. However, we expect households' purchasing power to be maintained through wage growth (after collective wage agreements and increases in the minimum wage). The government formally requested EUR84 billion in NGEU loans from the European Commission – adding to the grants already requested and received – which will support investment.

Spanish inflation has fallen much more quickly than in other large eurozone countries, with headline inflation of just 2.9% in May. Harmonised core inflation is also around 4%, below the eurozone average of 5.4%. However, as the base of comparison becomes more challenging we expect the inflation rate to rise slightly by end-2023 before resuming a downtrend in 2024. Household energy price inflation started to turn negative on an annual basis in October 2022, subtracting more than 1.4pp from the headline HICP rate by May 2023, while it was still contributing +0.5pp in the eurozone.

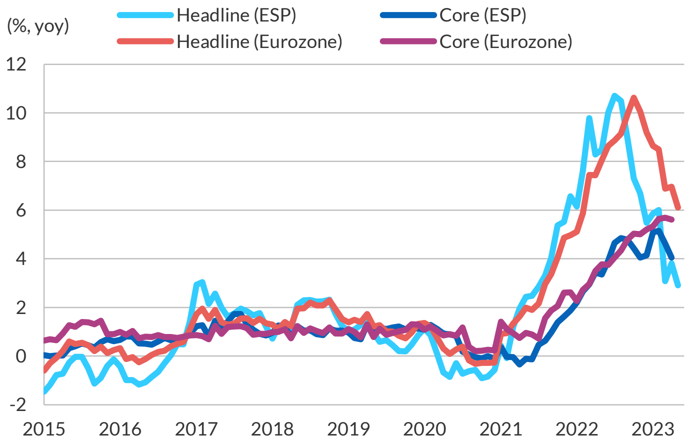
Spain's structural rate of unemployment is higher than that of the eurozone, with long-term unemployment 2.2pp higher than the average for the bloc. Looser labour market conditions should also reduce inflationary pressure. Unemployment fell to 12.7% in April, down 0.2pp yoy, and we expect it to continue to fall.

Spain - International Tourist Arrivals



Source: Fitch Ratings, UNWTO

Spain - Headline and Core Inflation vs Eurozone



Source: Fitch Ratings, Eurostat, Haver Analytics

Spain - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	0.8	5.4	1.9	1.6	1.8
Consumer spending	0.2	4.4	1.0	1.8	1.4
Fixed investment	1.3	4.6	1.5	3.5	2.4
Net trade (contribution pp)	0.0	2.3	0.5	-0.3	0.5
CPI inflation (end-year)	2.7	5.5	3.9	2.3	2.0
Unemployment rate	14.5	12.9	12.7	12.7	12.3
Policy interest rate (end-year)	0.15	2.50	4.50	3.75	3.00
Exchange rate, EURUSD (end-year)	1.14	1.07	1.09	1.09	1.09

Source: Fitch Ratings

Switzerland

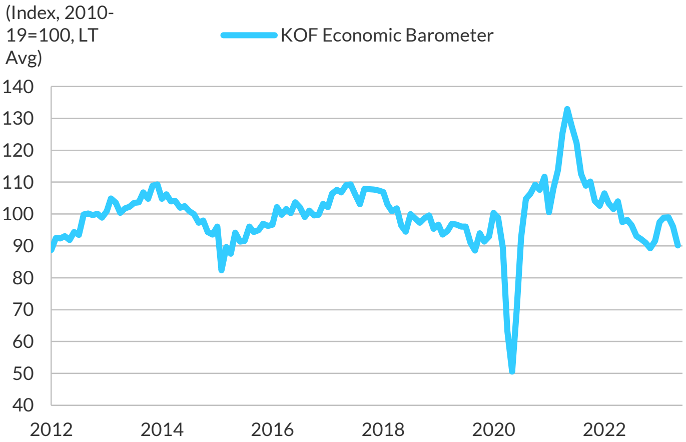
We have maintained our growth forecast for Switzerland at 0.8% in 2023 despite an unexpectedly strong performance in 1Q23; consumption grew 0.6% qoq and the tourism sector benefitted from the ongoing recovery in international travel. A rise in imports led to a net negative trade contribution. Subdued global growth will weigh on activity in Switzerland.

Survey data and business sentiment suggest that the pace of growth will subside during the rest of 2023. New orders in manufacturing are weakening, while the outlook for services is brighter. The KOF Economic Barometer declined across all sectors in May, and an official weekly activity indicator started to point to a yoy contraction. Bank credit is continuing to grow at a steady sequential pace. We expect a slight acceleration in growth in 2024 in line with the euro area, and above-trend growth in 2025. The key risks to the forecast include shocks to energy prices or supply, or to financial stability resulting from higher interest rates.

Inflation has come down slightly more quickly than the SNB had expected at its most recent policy meeting in March, falling to 2.2% (HICP) in May. Household energy prices are no longer increasing. Nevertheless, inflation remains above a conservative target of sub-2%, and there are further pressures in the pipeline in the form of indexed rents. The labour market continues to be tight. Wages grew at an annual 1.8% in 1Q23, three times the average growth rate in 2012-2021, but consistent with the growth in 1H22.

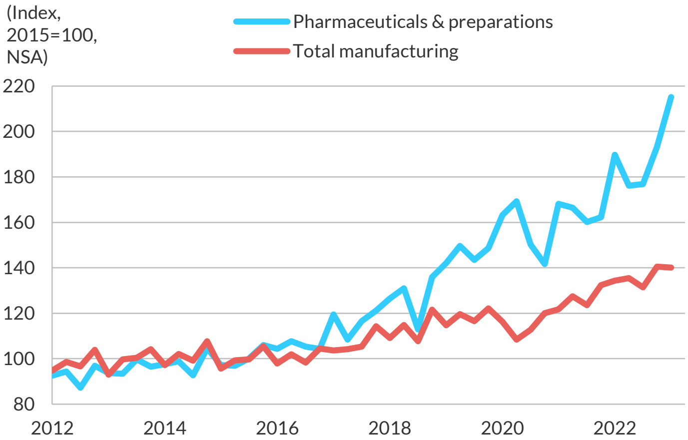
We have revised up our call for interest rates, expecting the SNB (which has only four scheduled monetary policy meetings a year) to raise rates by 50bp by end-2023. This would put our SNB call in line with the extra rate rises we now expect from the ECB. There are few signs of an outright recession that would dissuade the central bank of pursuing a further rate rise. The rate peak in Switzerland of 2% would be substantially less than in the eurozone, but inflation has been much lower and inflation expectations are anchored below 2%. The SNB has also used exchange-rate interventions to support the Swiss franc and lower inflation, a tool rarely used by most major central banks.

Switzerland - KOF Economic Barometer



Source: Fitch Ratings, Swiss Institute for Business Cycle Research, Haver Analytics

Switzerland - Industrial Production



Source: Fitch Ratings, SFSO, Haver Analytics

Switzerland - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	1.6	2.1	0.8	1.5	1.9
Consumer spending	0.7	4.0	1.8	1.2	1.3
Fixed investment	0.5	-0.3	1.4	1.3	1.6
Net trade (contribution pp)	1.1	0.9	-0.2	0.6	0.9
CPI inflation (end-year)	0.8	2.8	2.3	2.0	1.5
Unemployment rate	2.6	2.2	2.0	2.0	2.1
Policy interest rate (end-year)	-0.63	1.00	2.00	1.75	1.50
Exchange rate, USDCHF (end-year)	0.96	0.92	0.96	0.96	0.96

Source: Fitch Ratings

Australia

The 0.2% qoq expansion in GDP in 1Q23 was in line with our March GEO forecast. It reflected a strong increase in non-mining business investment that was largely offset by weak net trade as import growth outpaced that of exports. But dwellings investment contracted for the second consecutive quarter, while consumer spending growth slowed again, to +0.2% qoq, suggesting that monetary policy tightening is weighing on domestic demand.

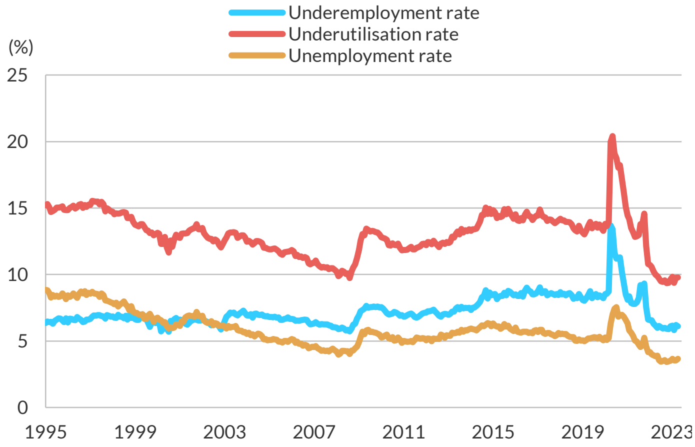
The latest business and consumer surveys suggest that economic growth remained feeble into 2Q23. Consumer confidence fell sharply in May, to 79.0, only marginally above the pandemic-era low. This deterioration probably reflects the additional tightening by the RBA, which unexpectedly raised the cash rate by 25bp to 4.10% in June, and signalled that further rate rises may be needed.

Headline inflation has remained too high for the RBA's comfort, easing only to 7.0% in 1Q23. Base effects mean that the headline rate will fall, to 4.2% by year-end and 2.8% by end-2024. But the core rate is likely to remain stickier, helped by the strength of the labour market. Unit labour costs, a key focus of the RBA, have shot up in recent quarters due to weak productivity growth. As a result, we expect the RBA to follow through on its hawkish rhetoric and raise the cash rate twice more, to 4.60%.

That additional tightening relative to our March forecast will push up the debt service burden on Australian households, many of whom are on variable-rate mortgages. Last year, they were able to fund their spending in part by running down savings built up during the pandemic. But in 1Q23, the household savings rate fell to 3.7%, below its 2015-2019 average.

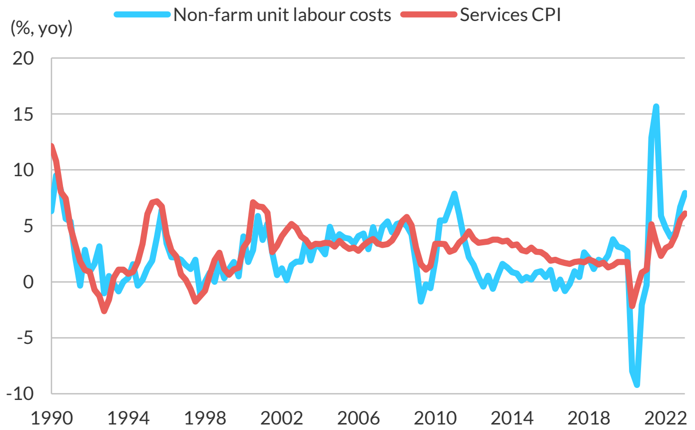
Investment is also likely to be dampened by higher interest rates. Residential investment has fallen for six consecutive quarters and the timelier building approvals data suggest that this weakness will persist. Meanwhile, although firms have raised their investment spending plans, this largely reflects higher input costs. Slower world trade may weigh at the margin on Australia's goods exports but this is likely to be offset by strong services exports for tourism and education. The rapid rebound in immigration is also supportive of aggregate growth. We expect GDP growth of 1.5% in 2023 and 2024, before a recovery to 2.2% in 2025, which would be a little bit above our estimate of potential growth.

Australia - Labour Market Indicators



Source: Fitch Ratings, ABS, Haver Analytics

Australia - Unit Labour Costs and Services CPI



Source: Fitch Ratings, ABS, Haver Analytics

Australia - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	2.4	3.7	1.5	1.5	2.2
Consumer spending	1.8	6.4	1.6	1.3	1.7
Fixed investment	1.7	1.1	1.4	1.7	2.9
Net trade (contribution pp)	-0.3	-1.5	0.7	0.2	0.2
CPI inflation (end-year)	2.7	8.4	4.2	2.8	2.0
Unemployment rate	5.2	3.7	4.0	4.4	4.2
Policy interest rate (end-year)	0.88	3.10	4.60	4.00	3.25
Exchange rate, USDAUD (end-year)	1.40	1.48	1.50	1.45	1.40

Source: Fitch Ratings

Canada

The 0.8% qoq growth in Canada's GDP in 1Q23 was stronger than expected, and reflected big increases in consumer spending and a positive contribution from net trade, even as investment contracted for the sixth consecutive quarter.

The preliminary GDP estimate for April from Statistics Canada, alongside solid business surveys for May, suggest that the economy expanded further in 2Q23, albeit less strongly than in the prior quarter. Housing market indicators also suggest some relief for the residential property market, with house prices rising mom in both April and May according to the Canadian Real Estate Association. Strong immigration is also supporting housing demand.

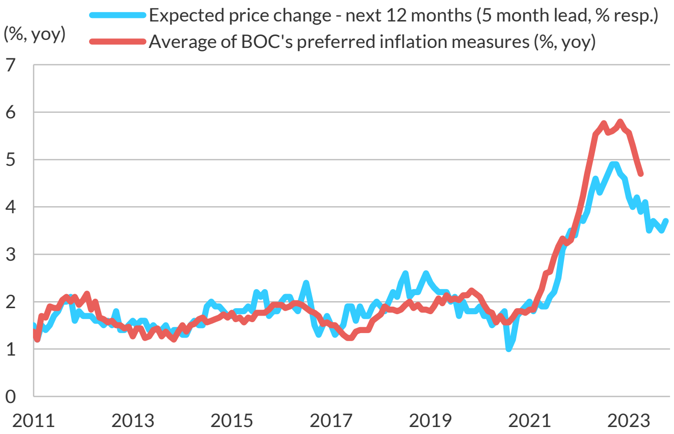
Nevertheless, Canada's economy still faces challenges and we expect these to cause GDP growth to slow later in 2023 and into 2024. Canada's exports are likely to struggle as the US economy enters recession in 4Q23, given their close links with the US business cycle. That said, the later timing of the recession in the US, combined with Canada's economic resilience in 1Q23, means that we have raised our GDP growth forecast for 2023 and lowered our 2024 projection, relative to what we expected in March.

On the domestic front, past tightening in monetary policy is taking its toll on residential investment and on households' finances. Household debt interest payments have already increased and the BOC estimates that by end-2024 almost two-thirds of mortgage holders will have seen their payments rise since February 2022.

Admittedly, headline inflation is subsiding and is likely to continue to do so, given falls in commodity prices and the easing of global supply chains. But underlying domestic price pressures are not disappearing quickly enough for the BOC, which unexpectedly resumed its tightening cycle in June after being on hold since late January.

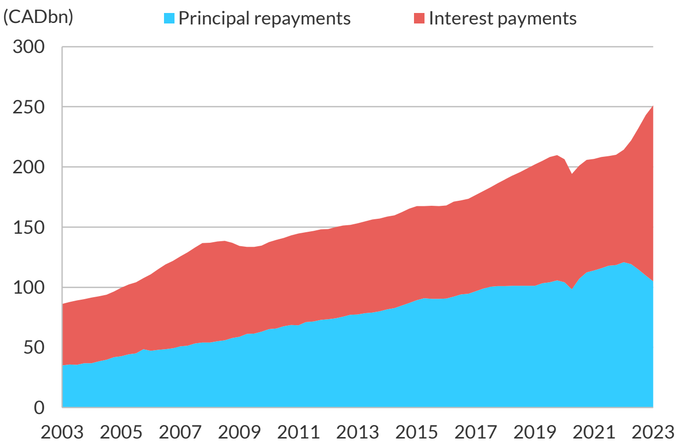
Recent signs of loosening in the labour market in May are unlikely to be sufficient to convince the BOC that it can return to the sidelines. The unemployment rate remains close to a multi-decade low, at 5.0%, even as labour participation has risen. Inflation expectations among consumers and firms are still well above target. Accordingly, we expect a further 25bp rate rise in July, to 5.0%, before an extended pause into 2024. We expect the BOC to cut its policy rate to 3.0% by end-2025, by which time headline inflation is likely to be back to target.

Canada - Inflation & Firms' Selling Price Expectations



Source: Fitch Ratings, Statistics Canada, CFIB, Haver Analytics

Canada - Household Debt Service Payments



Source: Fitch Ratings, Statistics Canada, Haver Analytics

Canada - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	1.6	3.4	1.3	0.8	2.0
Consumer spending	1.6	4.8	2.2	0.9	1.6
Fixed investment	1.4	-1.5	-2.8	1.1	2.7
Net trade (contribution pp)	-0.5	-1.5	1.7	-0.2	0.3
CPI inflation (end-year)	3.0	6.3	3.7	2.5	2.0
Unemployment rate	6.8	5.3	5.3	5.8	5.5
Policy interest rate (end-year)	1.20	4.25	5.00	4.00	3.00
Exchange rate, USDCAD (end-year)	1.30	1.36	1.35	1.35	1.35

Source: Fitch Ratings

Brazil

Fitch has raised its projection for 2023 real GDP growth to 2.3%, from 0.7%. A bumper agricultural harvest, which already drove a strong 1Q23 print and should also be supportive in 2Q23, was the main driver of this significant upward revision. Domestic demand continues to show signs of cooling amid tight monetary policy, but it has remained fairly resilient due to a strong labour market and fiscal loosening under the new Lula administration (which took office in January 2023).

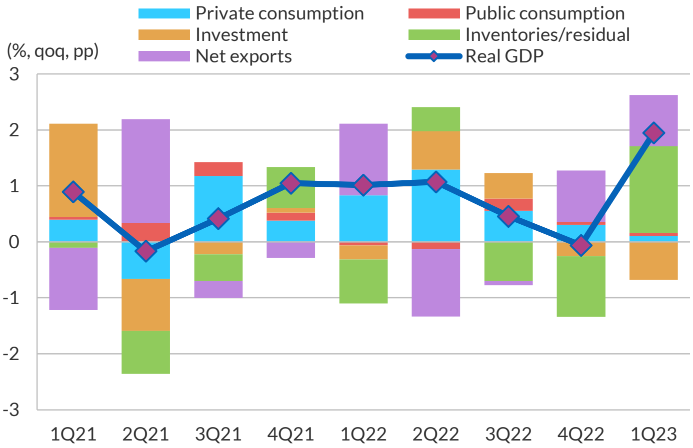
Fitch projects growth will ease to 1.3% in 2024, assuming normalisation in agricultural output. Tight monetary policy will continue to pose a drag on growth, but this should ease (with a lag) after interest rates are cut later in 2023. Market concerns around the policy direction under the Lula administration also appear to be easing somewhat, as its plans (fiscal, quasi-fiscal, micro) continue to take shape, but have not signalled intentions for radical changes. A new fiscal framework pending legislative approval has not fully anchored fiscal expectations, as it will rely on numerous tax measures subject to some uncertainty, but has allayed concerns around major slippage.

Inflation fell to 3.9% yoy in May 2023, and Fitch projects it will rise moderately to 5.2% by end-2023 (above the target of 3.25%+/-1.5pp) partly reflecting base effects from last year's fuel tax cuts being phased out. There is also some inertia to recent high inflation posed by indexation including a rise in the minimum wage.

The central bank (BCB) has kept its policy rate at 13.75%, and Fitch expects it to initiate cuts starting in 3Q23, with the SELIC rate reaching 12.25% by year-end. Inflation expectations rose earlier in 2023 amid fiscal and monetary policy uncertainty, reinforcing the BCB's hawkish stance, but have since stabilised and fallen somewhat, which should support a loosening cycle. The administration's desire to modify the inflation-targeting regime now appears more likely to focus on the horizon of convergence to the target rather than the target itself, and this should be clearer in the National Monetary Council's upcoming June meeting.

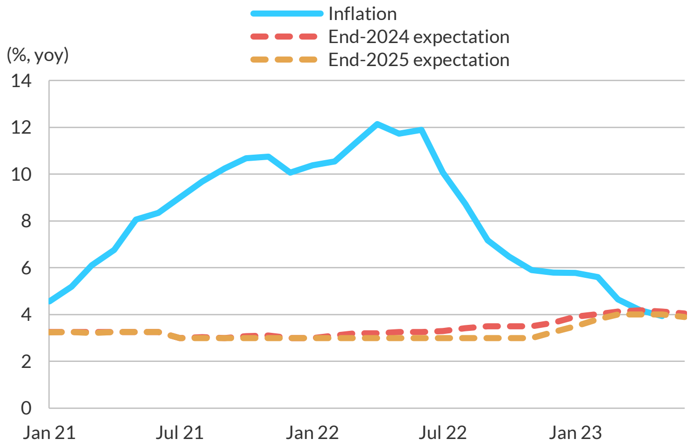
The Brazilian real has strengthened to BRL/USD 4.8 as of mid-June from BRL/USD 5.2 at end-2022, in line with a broader EM trend and reflecting some easing of market concerns around the domestic policy outlook. Fitch expects the real will depreciate to BRL/USD 5.1 by year-end as domestic monetary policy is loosened, and this could be sensitive to further definitions around fiscal policy.

Brazil - GDP and Components



Source: Fitch Ratings, IBGE, Haver Analytics

Brazil - Inflation and Inflation Expectations



Source: Fitch Ratings, BCB, Focus market survey, Haver Analytics

Brazil - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	1.5	2.9	2.3	1.3	2.1
Consumer spending	1.7	4.3	1.6	1.4	2.4
Fixed investment	5.0	0.8	-2.0	2.3	2.4
Net trade (contribution pp)	0.0	0.7	1.0	-0.1	0.0
CPI inflation (end-year)	5.6	5.8	5.2	4.0	4.0
Policy interest rate (end-year)	6.55	13.75	12.25	9.00	9.00
Exchange rate, USDBRL (end-year)	4.66	5.22	5.10	5.20	5.25

Source: Fitch Ratings

Russia

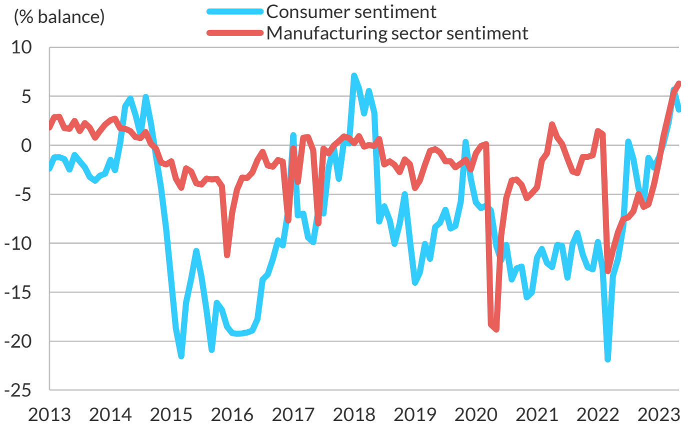
The economy continued to recover on a sequential qoq basis in 1Q23 with a stronger-than-expected outcome relative to our March forecast. On a non-seasonally adjusted yoy basis, the economy contracted 1.8% instead of the -5.1% yoy anticipated in the March GEO. Growth momentum has continued into 2Q23 with manufacturing and services sector PMIs remaining expansionary and above pre-invasion of Ukraine levels. Business and consumer sentiment as well as retail sales have increased while a recovery in mortgage and non-mortgage lending is underway. We now expect the economy to grow by 0.4% in 2023, a significant upgrade on the 1.4% contraction we had expected in March. For 2024 and 2025, we see growth of 1.4% and 1.5%, respectively.

Despite the better growth forecast for this year, ongoing international sanctions and significant structural changes will hinder potential growth in the medium term while local business will have to continue to rebuild supply chains and international business partnerships. While the manufacturing sector has shown resilience, the recent PMI index highlighted that firms have experienced a further sharp extension to supplier delivery times amid logistics challenges and disruptions.

Labour market dynamics also reflect some of the challenges facing the economy. Demand for labour has continued to grow as unemployment fell to record lows with companies facing growing recruitment difficulties. The number of vacancies continues to increase with a recent survey reporting that 35% of industrial companies questioned were facing labour shortages. Private investment activity remains high but is likely to be hampered by restrictions on investment imports, cancellation of joint projects with international companies and limited access to technology.

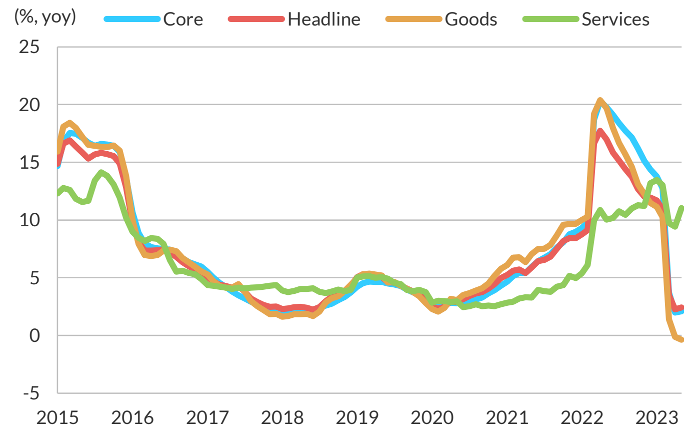
Annual headline inflation has decelerated rapidly in the past year slowing to 2.5% in May with core CPI also dropping to a similar rate though services sector inflation remains high. We expect the headline rate to pick up in 2H23 as a result of last year's negative month-on-month inflation prints dropping out of the annual measure. Underlying inflationary pressures are expected to persist given labour market imbalances. Policy rates have remained at 7.5% since September 2022 and we forecast a further increase to 8% partly reflecting a more hawkish tone in the central bank's June statement which said that "the overall balance of inflation risks has tilted even more to the upside".

Russia - Confidence Indices



Source: Fitch Ratings, CBRF, Rosstat, Haver Analytics

Russia - CPI Inflation Measures



Source: Fitch Ratings, CBRF, Rosstat, Haver Analytics

Russia - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	1.2	-2.1	0.4	1.4	1.5
Consumer spending	2.1	-1.4	1.3	1.3	1.8
Fixed investment	2.0	3.3	-0.1	-2.0	-0.9
Net trade (contribution pp)	-0.3	-1.1	-2.2	0.9	0.5
CPI inflation (end-year)	6.2	11.9	5.0	5.0	3.5
Policy interest rate (end-year)	7.32	7.50	8.00	6.50	5.00
Exchange rate, USDRUB (end-year)	68.33	70.34	83.00	85.00	87.00

Source: Fitch Ratings

India

Growth on a non-seasonally adjusted basis in 1Q23 was higher than expected at 6.1% yoy relative to our forecast of 4.3% yoy. This means that growth for the fiscal year ending in March 2023 was 7.2%, a slowdown from the 9.1% in the previous fiscal year. The breakdown by industry showed a recovery in manufacturing, after two consecutive quarterly contractions, a boost from construction and an increase in farm output. In expenditure terms, GDP growth was driven by domestic demand and a boost from net trade. Recent high-frequency data point to sustained near-term momentum as highlighted by rising PMI indices, higher car sales and increased power consumption. The economy also continues to benefit from high bank credit growth and infrastructure spending (with more to come from the latter).

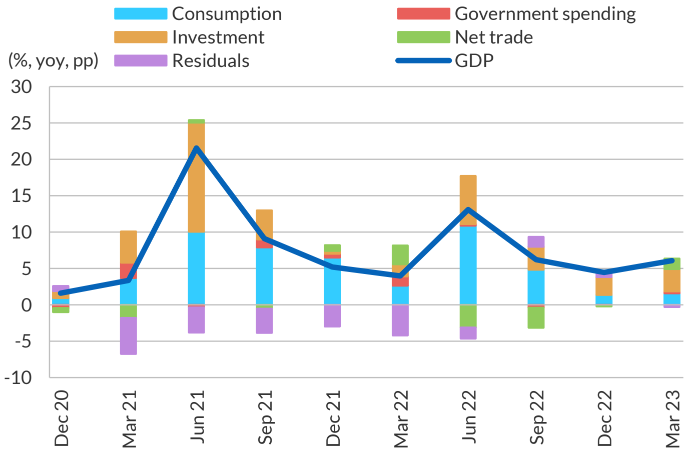
The stronger outturn in 1Q23 and near-term momentum have prompted us to upgrade our FY23-24 growth forecast to 6.3% – revised up from 6.0% in March – one of highest growth rates in the world.

India's economy will be affected to an extent by slowing global trade. Domestically the full impact of 250bp of monetary tightening is still to be felt. Consumers have also experienced a drop in purchasing power as inflation increased sharply in 2022 and household balance sheets have also been weakened through the pandemic. At the same time, the government's push on increased capital expenditure, moderation in commodity prices and robust credit growth are expected to support investment. Slowing inflation should also start to help consumers over time and households have now turned more optimistic about future earnings and employment.

The Reserve Bank of India (RBI) has kept policy rates at 6.5% since the start of the year, while headline inflation has eased from a peak of 7.8% to 4.3% in May, a figure that is already within the RBI's tolerance band of 4% target +/-2%. Wholesale price inflation (WPI) has also fallen to its lowest in more than seven years, to an annual rate of minus 3.5% in May. Nevertheless, while inflation has eased there are near-term upward risks in 2H23, given the monsoon outlook and the potential impact of El Niño.

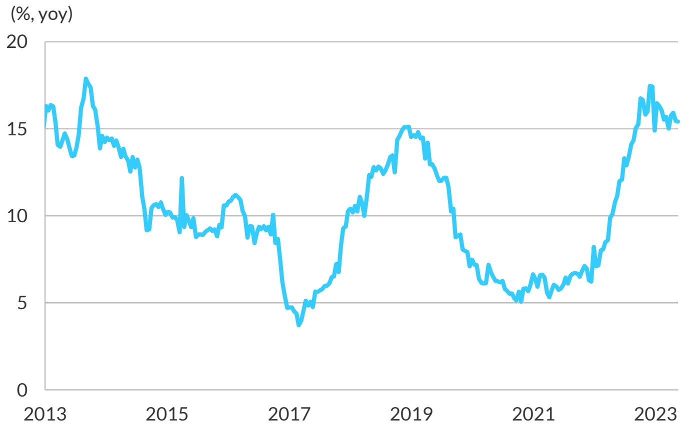
With growth expected to moderate further, and inflationary pressures easing, we expect the RBI to pause its rate cycle for the time being before cutting early next year – a change from our previous call of one more 25bp increase to 6.75%.

India - Contributions to Annual GDP Growth (NSA)



Source: Fitch Ratings, CSO, Haver Analytics

India - Bank Credit (Scheduled Commercial Banks)



Source: Fitch Ratings, Reserve Bank of India, Haver Analytics

India - Forecast Summary

(%) FY starting April	Annual Avg. 2018-2022	FY22-23	FY23-24F	FY24-25F	FY25-26F
GDP	4.2	7.2	6.3	6.5	6.5
Consumer spending	5.2	7.5	2.3	3.8	5.1
Fixed investment	6.2	11.4	9.9	9.5	7.4
Net trade (contribution pp)	0.2	-1.0	1.9	0.5	0.4
CPI inflation (end-cal. year)	5.2	5.7	5.0	4.7	4.5
Policy interest rate (end-cal. year)	5.04	6.25	6.50	5.75	5.75
Exchange rate, USDINR (end-cal. year)	73.09	82.79	82.00	82.00	82.00

Source: Fitch Ratings

Korea

The 0.3% qoq expansion in Korea's GDP in 1Q23 was in line with our forecast in March's GEO. Consumer spending rebounded after contracting in the previous quarter, while net trade also made a small positive contribution to growth. This was partially offset by a fall in investment.

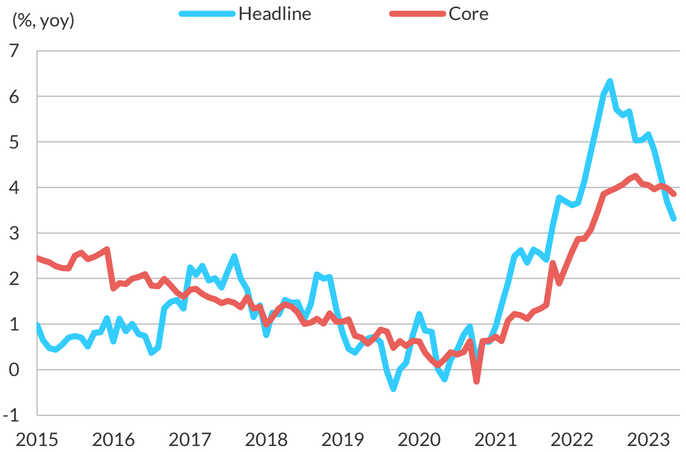
Timely export data suggest that the external sector struggled in 2Q23 and we expect this to continue given the weakness in world trade that we expect this year. Semiconductor shipments fell sharply in April, down 32.5% yoy. The manufacturing inventories-to-shipments ratio has climbed further, to its highest level since the early 1980s. This suggests that once demand revives, producers will be able to run down stocks first before boosting output.

The domestic economy is also likely to struggle this year, facing the challenges of the lagged impact from the cumulative 300bp of policy tightening. More than 70% of outstanding mortgage loans are based on floating interest rates, so indebted households are facing higher interest payments. Banks are especially tightening lending standards on mortgage loans, and a combination of higher rates and oversupply in some areas have taken their toll on house prices. But firms are also affected by tighter credit conditions – SMEs in particular. That, alongside the slowdown in world trade, will weigh on investment. We expect GDP to expand by 1.2% in 2023 before a recovery to 2.5% in 2024 and 2.7% in 2025.

Nevertheless, the challenge to the domestic economy from higher inflation has eased, with headline CPI falling to 3.3% yoy in May. The core (ex-food and energy) rate has been stuck at about 4%, but we expect this to fall in 2023, as re-opening inflation subsides. We now expect headline inflation to end 2023 at 1.8% and to fall further over the course of 2024 and 2025.

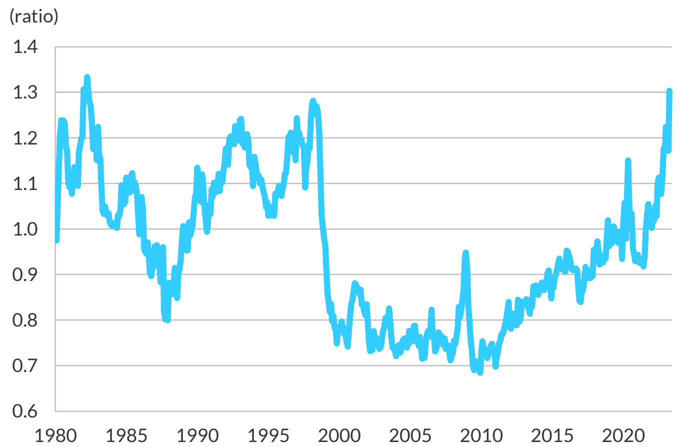
With inflation subsiding and economic growth weakening, we expect the Bank of Korea (BoK) to keep rates on hold at 3.50%. But the hawkish tone from Governor Rhee Chang Yong and the focus on core inflation suggests that interest rates will remain elevated this year. Our base case is that the BoK will not start to cut rates until 2024, but that loosening could come sooner given subdued growth and declining inflation.

Korea - Inflation Measures



Source: Fitch Ratings, Statistics Korea, Haver Analytics

Korea - Manufacturing Inventories-to-Shipments Ratio



Source: Fitch Ratings, Statistics Korea, Haver Analytics

Korea - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	2.3	2.6	1.2	2.5	2.7
Consumer spending	1.6	4.1	2.1	1.8	2.0
Fixed investment	0.4	-0.5	2.0	2.6	3.2
Net trade (contribution pp)	0.7	0.2	-1.0	0.6	0.4
CPI inflation (end-year)	2.0	5.0	1.8	1.5	1.2
Policy interest rate (end-year)	1.31	3.25	3.50	3.00	2.50
Exchange rate, USDKRW (end-year)	1,176	1,267	1,350	1,350	1,350

Source: Fitch Ratings

Indonesia

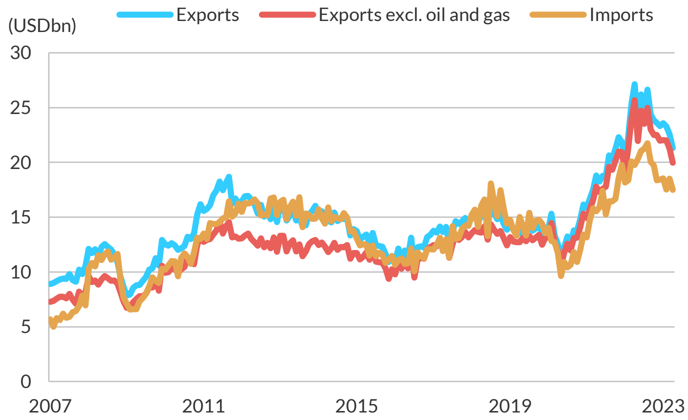
Growth in 1Q23 beat our March GEO forecast as consumer and government spending more than offset a slowdown in exports and investment. The 5% yoy non-seasonally adjusted increase exceeded the 4.3% yoy we expected, and while the economy is likely to lose some momentum, the magnitude of the outperformance in 1Q23 has prompted us to upgrade our 2023 growth projection by 0.2pp to 5%.

The economy will start to face challenges from lower commodity prices, a total of 225bp of cumulative monetary tightening to date and weaker global demand. The May manufacturing PMI eased to 50.3 in May from 52.7, representing continued expansion but at a slower pace. The moderation in the overall index was driven by deterioration in new orders while the volume of new work fell for the first time in almost two years, albeit after rising at the fastest rate in seven months in April. Foreign demand also waned, with new orders from abroad falling for the 12th month in a row. Domestically, consumer confidence has increased in recent months and as inflation falls further, private consumption is likely to contribute solidly to overall economic growth. Investment activity continues to be dominated by non-building investment.

Headline annual inflation has declined rapidly, easing to 4.01% in May and is now at the top end of the central bank's 3% +/-1% target range. Lower energy and food prices compared to a year ago helped to push headline inflation lower across almost all categories in the CPI basket. Underlying inflation also continues to decline while inflation expectations remain anchored. Bank Indonesia now expects headline inflation to fall further towards the end of this year. Fitch expects inflation to end 2024 at 3%, within the BI's new lower inflation target range for next year of 2.5% +/-1%.

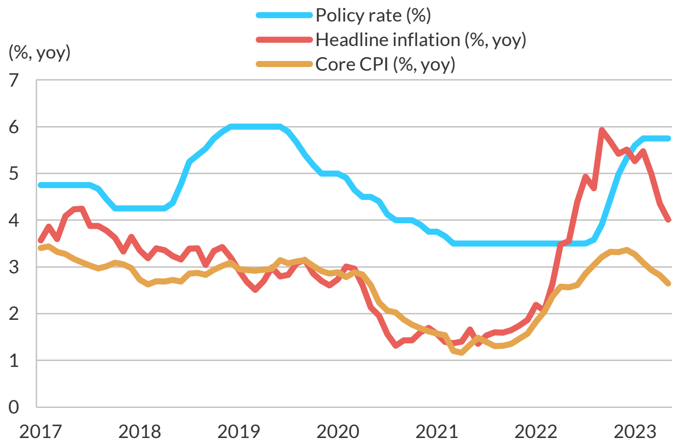
The recent strengthening of the rupiah will also help to dampen inflationary pressures. We expect the rupiah to remain supported by a positive current account balance and foreign capital inflows, the latter attracted by the promising economic growth outlook, low inflation and appealing yields on domestic financial assets. Fitch expects policy rates to remain at 5.75% for the remainder of this year – also helping to support the rupiah - before being cut early in 2024.

Indonesia - Trade in Goods



Source: Fitch Ratings, Badan Pusat Statistik, Haver Analytics

Indonesia - Inflation and Policy Rates



Source: Fitch Ratings, Badan Pusat Statistik, Bank Indonesia, Haver Analytics

Indonesia - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	3.4	5.3	5.0	5.2	5.0
Consumer spending	2.9	4.9	4.3	4.1	4.3
Fixed investment	2.8	3.9	4.3	5.7	5.4
Net trade (contribution pp)	0.5	0.8	1.4	1.0	0.7
CPI inflation (end-year)	2.8	5.5	3.0	3.0	2.5
Policy interest rate (end-year)	4.50	5.50	5.75	5.00	4.50
Exchange rate, USDIDR (end-year)	14,425	15,731	15,000	15,000	15,000

Source: Fitch Ratings

Mexico

We have raised our 2023 growth forecast by 0.9pp since the March GEO but we still forecast growth to slow to 2.5% this year. Growth of 1% qoq in 1Q23 outperformed our forecast of 0.2% by a wide margin. This year's growth will benefit from statistical carryover effects given the sustained quarterly growth in 2022, robust labour market performance and the ongoing recovery from the pandemic. Output is now 1.7% above the 4Q19 level.

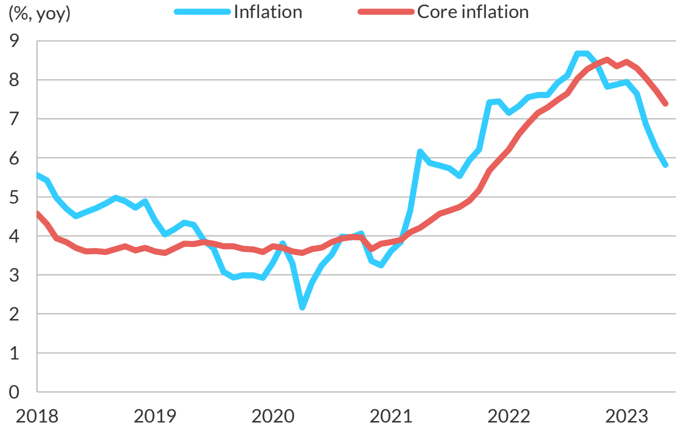
A strong labour market, coupled with robust remittance inflows, has supported private consumption, although persistently high inflation and a restrictive monetary policy stance may weigh on growth later this year. External demand continues to be supportive although the economy will be affected by the anticipated US economic slowdown, affecting manufacturing export demand and remittances flows.

Sluggish investment, which remains below its 2015 level in real terms, has hindered Mexico's economic growth, but machinery and equipment has shown sustained dynamism in recent quarters, hinting at increasing demand for Mexican manufacturing production, possibly due to nearshoring effects. Nearshoring remains an important growth opportunity for Mexico, given increased US-China tensions and manufacturers' desire for shorter and more resilient supply chains. Residential construction by contrast has been particularly slow to recover from a slump during the pandemic.

Inflation declined to 5.8% in May 2023 from its peak of 8.7% in September 2022. Core inflation has also begun to decline but at a more moderate pace, reaching 7.4% in May from its previous peak of 8.5% in November of last year. We forecast a gradual decline, helped by the lagged impact of earlier monetary tightening.

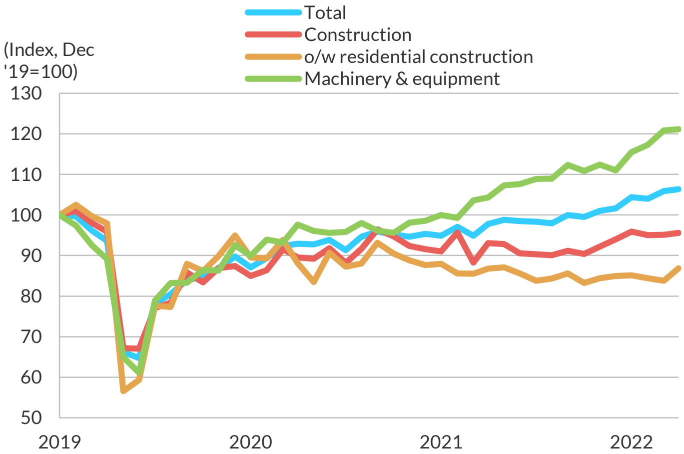
Banco de Mexico (Banxico) increased its policy rate by 725bps between May 2021 and March 2023 to anchor expectations amid the inflation surge. At the May 2023 meeting, Banxico policymakers decided to keep the policy rate unchanged at 11.25% after fifteen consecutive increases. We believe Banxico has ended its policy-tightening cycle and project the policy rate to remain at 11.25% until November before being cut to 11.00%. High ex-ante real interest rates will allow Banxico to ease its monetary policy rate ahead of the Federal Reserve. The policy rate differential has also helped lead to a steep appreciation of the currency, reflected in our revised exchange-rate forecast.

Mexico - Inflation



Source: Fitch Ratings, Banxico, Haver Analytics

Mexico - Investment



Source: Fitch Ratings, INEGI, Haver Analytics

Mexico - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	0.3	3.0	2.5	1.8	2.0
Consumer spending	1.3	6.1	2.1	1.8	2.0
Fixed investment	-1.0	6.0	3.9	1.9	1.5
Net trade (contribution pp)	-0.1	-0.5	-1.0	0.1	0.3
CPI inflation (end-year)	5.1	7.8	4.8	4.2	3.8
Policy interest rate (end-year)	6.66	10.50	11.00	9.25	7.50
Exchange rate, USDMXN (end-year)	20.08	19.41	18.30	19.00	19.50

Source: Fitch Ratings

Poland

Growth in 1Q23 was much stronger than expected on a non-seasonally adjusted basis at -0.3% yoy compared to -3.0% yoy in the March GEO. In seasonally adjusted terms, this equates to a quarterly rebound of 3.8%, which offset the sharp contraction in 4Q22. Recent GDP data have been highly volatile – with a massive decline in public consumption in 4Q22 that was fully reversed in 1Q23 – obscuring what is a weakening underlying growth picture.

Private consumption fell in 1Q23 and more recent monthly data suggest that high inflation continues to adversely affect consumers, with retail sales decreasing yoy. Household credit has also slowed rapidly reflecting weaker mortgage demand. This is unsurprising given the 665bp increase in policy rates in the past two years.

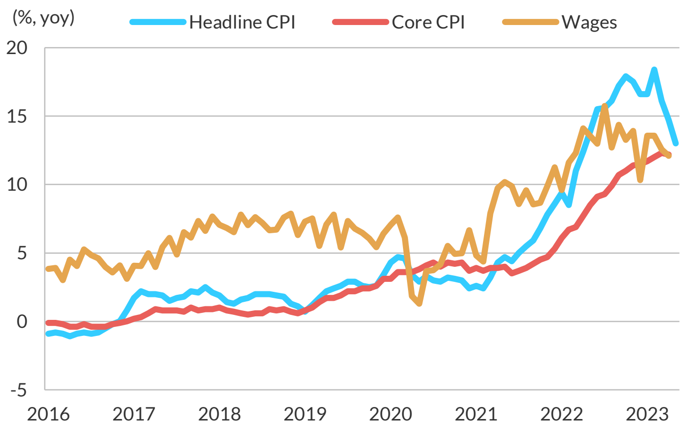
Lending to corporates is also decelerating rapidly. Investment has faced challenges from energy prices, higher interest rates and declining housing activity. The external environment has proved to be somewhat challenging given the slowdown in key trading partners and slowing global trade, although inward FDI is picking up.

We have kept our annual 2023 GDP forecast at 0.7%. We expect the economy to rebound in 2024 and 2025 as external shocks fade, headline inflation falls and real wage growth recovers, and expect growth of 2.8% in 2024 and 3.2% in 2025.

Headline CPI moderated to 13% yoy in May as food inflation eased, while the sectoral split showed disinflation in goods but little decline in services. The stabilisation in food and energy prices should lead to further declines in the headline rate. Core inflation remains high and its decline is likely to be more protracted. The labour market remains tight, annual wage growth still is in double-digits and there are proposals for a large increase in the minimum wage. That said, easing global supply-chain congestion, slowing domestic economic activity and the appreciation in the zloty should help inflation dynamics. The zloty has strengthened to around USDPLN 4.1 from a peak of 5.0 late last year.

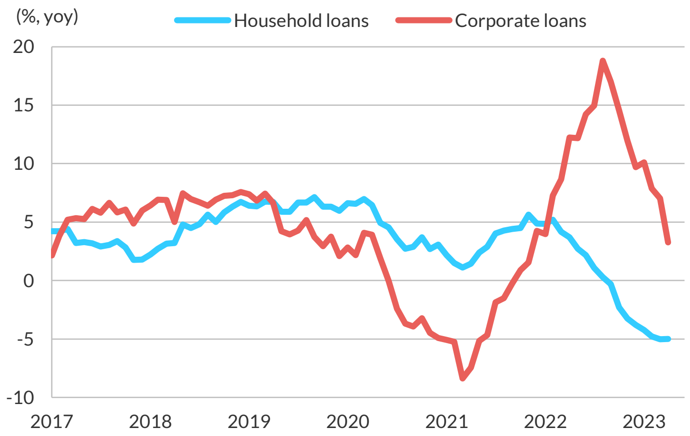
The NBP (central bank) has kept policy rates at 6.75% for 10 months and we expect they will remain at this level until early next year. This is in line with a number of other emerging-market central banks, which following earlier significant monetary policy tightening, are now keeping policy rates on hold.

Poland - CPI Inflation and Wages



Source: Fitch Ratings, CSO, National Bank of Poland, Haver Analytics

Poland - Household and Corporate Loans



Source: Fitch Ratings, National Bank of Poland, Haver Analytics

Poland - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	4.1	5.1	0.7	2.8	3.2
Consumer spending	2.6	3.3	-3.1	3.1	3.7
Fixed investment	4.3	5.0	5.0	3.6	2.8
Net trade (contribution pp)	0.2	0.2	2.4	-0.1	0.2
CPI inflation (end-year)	5.4	16.7	9.0	5.0	4.0
Policy interest rate (end-year)	1.83	6.75	6.75	5.00	4.50
Exchange rate, USDPLN (end-year)	3.93	4.40	4.30	4.30	4.30

Source: Fitch Ratings

Turkiye

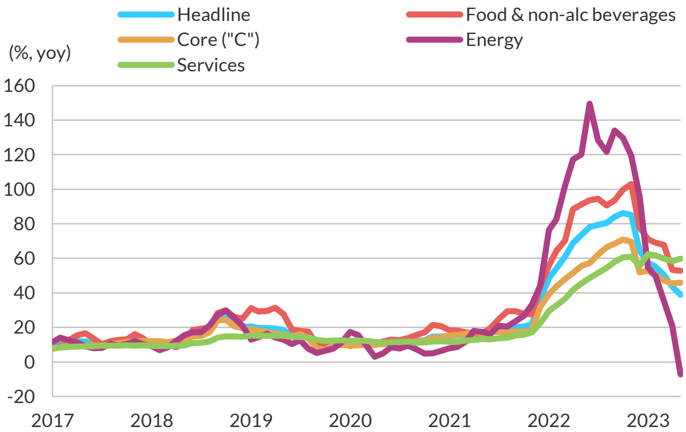
President Recep Tayyip Erdogan's appointment of both a new finance minister and a central governor after his re-election appears to raise the prospect of a return to more orthodox economic policies. Mehmet Simsek, the new finance minister, said that Turkiye will adopt "rational" policies and that a "rules-based, predictable Turkish economy will be the key to achieving the desired prosperity". Turkiye's mounting external imbalance, diminished FX reserves and the return to more orthodox economic measures imply a near-term increase in policy rates.

Over the past couple of years, the CBRT has implemented continuous policy rate cuts even as domestic inflation has surged and central banks elsewhere were tightening policy rates. The result of this policy has been a plunge in the country's currency from about TRYUSD 7.5 in early 2021 to about 23 now. Inflation in that period jumped from 20% to a peak of 86% late last year. In recent months, foreign-currency restrictions and central bank interventions have propped up the lira at an artificially strong level.

The promised shift to a more orthodox approach has raised the prospect of tighter monetary policy. We now expect the CBRT to implement a significant increase in policy rates at the MPC meeting on 22 June and raise its policy rate to 25% by end-2023 from 8.5% currently. We then expect the Central Bank of the Republic of Turkiye to leave rates on hold next year before cutting in 2025. Since Erdogan's election victory and the announced shift to more orthodox economic policies, the lira has depreciated sharply and we expect lira weakness to continue over the forecast horizon. Headline annual inflation has slowed from its peak last year to a still-high 39%, driven by declines in energy and goods components, but services inflation remains elevated, while core inflation has hardly moved down from very high levels.

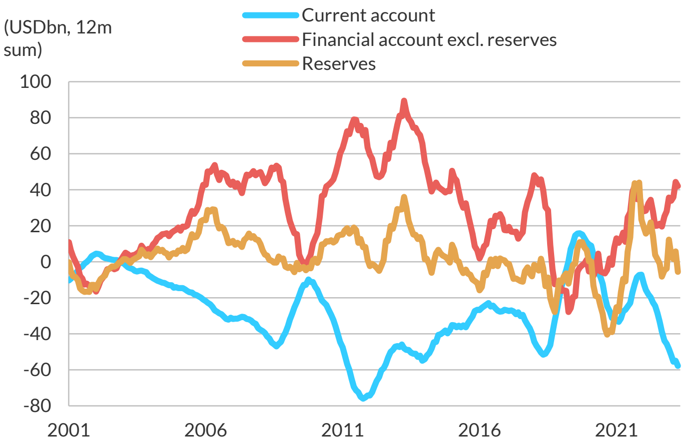
Growth in 1Q23 was largely in line with our expectations, increasing 0.3% qoq (March GEO 0.4% qoq) and driven by a pick-up in investment, a drop in net exports and an improvement in consumption. We have maintained our growth forecasts for this year and next, at 2.5% and 3%, respectively, before expecting a rise to 3.8% in 2025. Higher interest rates may slow credit growth, although this could be partially offset by the easing of some previously targeted macroprudential measures. But the recent weakening of the lira will boost net trade. Private consumption could also be supported by wage increases and improved confidence due to the expectation of a less interventionist approach. And while the pace of fiscal expansion is expected to ease, the post-earthquake reconstruction process will gather pace.

Turkiye - CPI Inflation Measures



Source: Fitch Ratings, Turkish Statistical Institute, Haver Analytics

Turkiye - Balance of Payments



Source: Fitch Ratings, CBRT, Haver Analytics

Turkiye - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	4.5	5.6	2.5	3.0	3.8
Consumer spending	8.0	19.6	8.6	1.9	2.6
Fixed investment	1.0	2.8	5.7	2.4	3.8
Net trade (contribution pp)	1.2	0.6	-2.2	0.7	0.5
CPI inflation (end-year)	27.1	64.3	45.0	35.0	25.0
Policy interest rate (end-year)	15.30	9.00	25.00	25.00	20.00
Exchange rate, USDTRY (end-year)	8.58	18.72	26.50	27.50	28.50

Source: Fitch Ratings

South Africa

The economy grew in line with our expectations in 1Q23 at 0.4% qoq, but we have lowered our expectation for growth this year as the domestic energy crisis persists, business confidence falls and interest rates increase more rapidly.

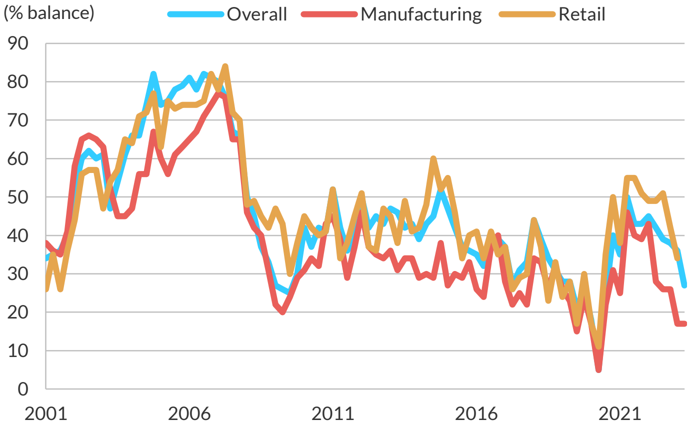
The expenditure breakdown of GDP showed that investment and government spending provided the bulk of growth in 1Q23 while private consumption recorded a relatively modest increase of 0.4% qoq. Business confidence recently posted a further decline and there is little sign that the domestic energy crisis is over. Moreover, commodity prices remain weak, external conditions are deteriorating and we expect that policy rates have further to rise after the central bank's recent hawkish turn.

We now expect no growth in 2023, revised down from our previous forecast of 0.4%. We expect consumer spending growth to remain low due to the squeeze on household incomes emanating from high inflation and higher interest rates. At the same time, the recent recovery in fixed investment is forecast to stall as economic growth prospects wane and risk perceptions worsen. Moreover, we see only a modest recovery of 0.9% in 2024. Growth should pick up slightly in 2025 – as interest rates fall and stepped up energy investment starts to gain momentum – but will remain fairly subdued at 1.3%.

Headline inflation has been slow to decline relative to its EM peers, and at 6.3% yoy remains outside the central bank's target range of 3%-6%. Higher food and energy prices have kept annual inflation elevated while core and services sector inflation continue to increase. Inflation risks have increased, driven by persistent power cuts (load-shedding) and recent weakness in the rand. The South African Reserve Bank (SARB) estimates that power cuts will add to inflation, with firms looking to pass on these higher costs to consumers. SARB said that back-up generators entail higher fuel costs, which are likely to be passed on to consumers.

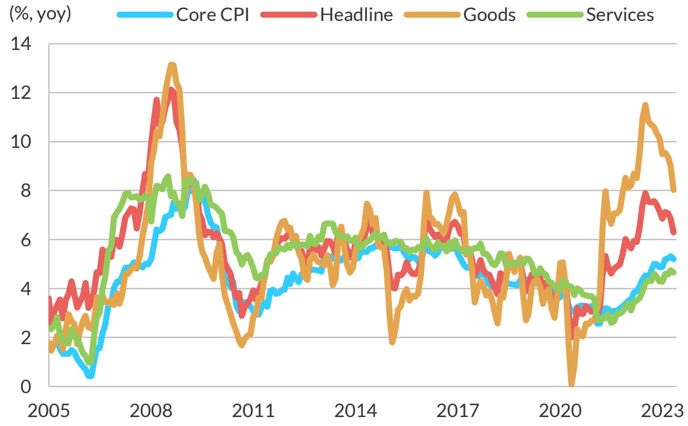
SARB surprised the market by raising interest rates to 8.25% in May expressing growing concerns about the adverse impact of the energy crisis on inflation and the risk of rising inflation expectations. While the rand subsequently strengthened, we expect a further 25bp increase in policy rates as inflation risks remain high and global interest rates increase again. Core inflation remained high at 5.2% in May and we have raised our end-2023 inflation projection to 6.0% from 5.6%.

South Africa - Business Confidence



Source: Fitch Ratings, Bureau for Economic Research, Haver Analytics

South Africa - Inflation Measures



Source: Fitch Ratings, Statistics South Africa, Haver Analytics

South Africa - Forecast Summary

(%)	Annual Avg. 2018-2022	2022	2023F	2024F	2025F
GDP	0.5	1.9	0.0	0.9	1.3
Consumer spending	1.3	2.5	0.7	1.0	1.1
Fixed investment	-2.4	4.8	3.2	1.7	2.6
Net trade (contribution pp)	-0.3	-2.0	-0.9	-0.1	0.0
CPI inflation (end-year)	4.7	7.2	6.0	5.0	4.0
Policy interest rate (end-year)	5.25	7.00	8.50	7.00	5.75
Exchange rate, USDZAR (end-year)	15.06	16.99	18.50	18.50	18.50

Source: Fitch Ratings

Appendix 1

Quarterly GDP QOQ

(%)	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	1Q24	2Q24
US	-0.4	-0.1	0.8	0.6	0.3	0.4	0.1	-0.9	-0.2	0.7
Eurozone	0.7	0.8	0.4	-0.1	-0.1	0.4	0.4	0.3	0.3	0.3
China	0.8	-2.3	3.9	0.6	2.2	0.7	1.3	1.4	1.2	1.2
Japan	-0.7	1.4	-0.4	0.1	0.7	0.3	0.3	0.2	0.2	0.2
UK	0.5	0.1	-0.1	0.1	0.1	-0.2	-0.3	0.0	0.4	0.6
Germany	1.0	-0.1	0.5	-0.5	-0.3	0.5	0.2	0.3	0.3	0.2
France	-0.1	0.5	0.2	0.0	0.2	0.2	0.3	0.3	0.3	0.4
Italy	0.1	1.0	0.4	-0.1	0.6	0.1	0.1	0.1	0.3	0.3
Spain	-0.4	2.5	0.4	0.4	0.5	0.3	0.1	0.3	0.5	0.5
Switzerland	0.3	0.3	0.2	0.0	0.3	0.3	0.3	0.3	0.4	0.4
Australia	0.6	0.8	0.6	0.6	0.2	0.2	0.2	0.2	0.4	0.5
Canada	0.6	0.9	0.6	0.0	0.8	0.1	0.0	0.0	0.1	0.4
Brazil	1.0	1.1	0.5	-0.1	1.9	-0.3	0.2	0.2	0.4	0.4
Russia	0.1	-4.4	0.7	0.5	0.7	0.3	-0.5	0.5	0.6	0.4
India	-0.2	0.3	2.7	1.4	1.3	1.8	1.4	1.3	1.2	2.0
Korea	0.7	0.8	0.2	-0.3	0.3	0.4	0.6	0.6	0.7	0.6
Mexico	1.0	1.1	0.9	0.6	1.0	0.2	0.2	0.3	0.6	0.6
Indonesia	1.4	1.1	0.9	1.5	1.5	0.9	1.2	1.3	1.4	1.4
Turkiye	0.7	1.8	-0.1	0.9	0.3	0.6	1.0	0.6	0.8	0.8
Poland	4.5	-2.5	1.0	-2.3	3.8	-2.0	0.3	1.1	0.9	1.0
South Africa	1.5	-0.8	1.8	-1.1	0.4	-0.3	0.0	0.2	0.4	0.4
Developed [a]	-0.1	0.3	0.5	0.3	0.3	0.3	0.1	-0.4	0.0	0.5
Emerging [b]	0.8	-1.4	2.7	0.5	1.8	0.6	1.0	1.1	1.1	1.1
Emerging ex-China	0.7	-0.1	1.1	0.4	1.2	0.5	0.6	0.7	0.8	1.0
World [c]	0.2	-0.3	1.3	0.4	0.9	0.4	0.4	0.2	0.5	0.8

[a] US, Japan, France, Germany, Italy, Spain, UK, Canada, Australia and Switzerland
[b] Brazil, Russia, India, China, South Africa, Korea, Mexico, Indonesia, Poland and Turkiye
[c] 'Fitch 20' countries weighted by nominal GDP in US dollars at market exchange rates (three-year average)
Source: Fitch Ratings

Appendix 2

Quarterly GDP YOY

(%)	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	1Q24	2Q24
US	3.7	1.8	1.9	0.9	1.6	2.1	1.4	-0.2	-0.7	-0.4
Eurozone	5.5	4.4	2.5	1.8	1.0	0.5	0.5	1.0	1.4	1.4
China	4.8	0.4	3.9	2.9	4.5	7.5	4.8	5.6	4.6	5.1
Japan	0.6	1.5	1.6	0.4	1.8	0.7	1.3	1.4	1.0	1.0
UK	10.6	3.8	2.0	0.6	0.2	0.0	-0.3	-0.4	-0.1	0.6
Germany	3.8	1.7	1.4	0.8	-0.5	0.1	-0.1	0.7	1.4	1.1
France	4.5	4.0	1.1	0.6	0.9	0.5	0.6	0.9	1.1	1.3
Italy	6.5	5.0	2.5	1.5	1.9	1.0	0.7	0.9	0.6	0.8
Spain	6.5	7.7	4.9	2.9	3.8	1.5	1.3	1.2	1.2	1.4
Switzerland	4.4	2.4	0.8	0.7	0.6	0.7	0.8	1.2	1.3	1.4
Australia	3.1	3.1	6.0	2.6	2.3	1.6	1.2	0.8	1.0	1.3
Canada	3.2	4.7	3.8	2.1	2.2	1.4	0.8	0.8	0.1	0.5
Brazil	2.4	3.7	3.6	1.9	4.0	2.0	1.8	2.1	0.5	1.2
Russia	3.0	-4.5	-3.5	-2.7	-1.8	2.2	1.0	1.0	0.9	1.1
India	4.0	13.1	6.2	4.5	6.1	7.4	6.0	5.9	5.8	6.0
Korea	3.1	2.9	3.2	1.4	0.9	0.7	1.1	2.0	2.4	2.6
Mexico	1.9	2.4	4.3	3.5	3.7	2.7	2.0	1.7	1.2	1.6
Indonesia	5.0	5.5	5.7	5.0	5.0	4.8	5.1	5.0	4.9	5.3
Turkiye	7.6	7.8	4.0	3.5	4.0	1.8	2.8	2.5	2.9	3.1
Poland	8.8	6.1	3.9	2.3	-0.3	0.3	-0.3	3.1	0.3	3.3
South Africa	2.5	0.2	4.1	0.8	0.2	0.7	-1.1	0.2	0.3	0.9
Developed [a]	4.0	2.5	2.1	1.0	1.4	1.4	1.0	0.3	0.0	0.3
Emerging [b]	4.4	2.3	3.7	2.6	3.8	5.8	3.9	4.5	3.8	4.3
Emerging ex-China	3.8	5.0	3.4	2.3	2.9	3.3	2.7	3.0	2.6	3.1
World [c]	4.2	2.5	2.7	1.6	2.4	3.1	2.2	2.0	1.5	1.9

[a] US, Japan, France, Germany, Italy, Spain, UK, Canada, Australia and Switzerland
[b] Brazil, Russia, India, China, South Africa, Korea, Mexico, Indonesia, Poland and Turkiye
[c] 'Fitch 20' countries weighted by nominal GDP in US dollars at market exchange rates (three-year average)
Source: Fitch Ratings

Contacts

Economics

Brian Coulton
Chief Economist
+44 20 3530 1140
brian.coulton@fitchratings.com

Olu Sonola
+1 212 908 0583
olu.onola@fitchratings.com

Jessica Hinds
+44 20 3530 2213
jessica.hinds@fitchratings.com

Robert Ojeda-Sierra
+44 20 3530 1664
robert.ojeda-sierra@fitchratings.com

Pawel Borowski
+44 20 3530 1861
pawel.borowski@fitchratings.com

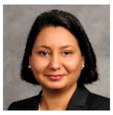
Charles Seville
+44 20 3530 2642
charles.seville@fitchratings.com

Sovereign Ratings

Todd Martinez
Americas
+1 212 908 0897
todd.martinez@fitchratings.com

Thomas Rookmaaker
Asia
+852 2263 9891
thomas.rookmaaker@fitchratings.com

Federico Barriga Salazar
Western Europe
+49 69 768 076 145
federico.barrigasalazar@fitchratings.com



Shelly Shetty
Americas
+1 212 908 0324
shelly.shetty@fitchratings.com

Paul Gamble
Emerging Europe
+44 20 3530 1623
paul.gamble@fitchratings.com

Jan Friederich
Middle East and Africa
+852 2263 9910
jan.friederich@fitchratings.com